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The Importance of Promptly Presenting Checks for Payment

WILLIAM O. MORRIS*

The importance of the use of checks in the commercial world may well be illustrated by comparison of the following statistics. As of December 31, 1957, there was in circulation in United States currency, outside of the Treasury, $31,834,367,367,[1] or $184.24 for every man, woman, and child in the United States.[2] As of the same date, the total bank deposits in the 14,088[3] banks in this country totalling $233,630,000,000,[4] of which $128,420,000,000 was represented by demand deposits.[5] As staggering as these sums appear, the amount of outstanding currency at the end of 1957 was relatively small when we consider that the debits to demand deposits, except interbank and United States Government accounts, for 1957 was $2,356,768,000,000[6] representing debits for each of our estimated 160,000,000 population for the year of $14,729, or almost seventy-five times the sum of all outstanding currency. When it is observed that many checks may well have passed through several transactions before being paid by the drawee, the amount of the debts discharged by checks would exceed an amount beyond the comprehension of most persons.

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This article is reprinted with the permission of the editors of the WEST VIRGINIA LAW REVIEW, published by the West Virginia University, Morgantown, W. Va. Certain portions of the full article relating solely to West Virginia law have been omitted.

[1] CIRCULATION STATEMENT OF U.S. MONEY, TREASURY DEPARTMENT—Fiscal Service—Office of the Treasurer of the United States (1958).

[2] Based on Bureau of Census estimated population.

[3] 44 ANN. REP. BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM 1957, table 16, p. 103 (1958).

[4] *Ibid.*

[5] *Ibid.*

[6] FEDERAL RESERVE BULLETIN, September, 1958, p. 1078.

Considering the number of checks written each year and amount of money thereby represented, it is indeed the eighth wonder of the world that the courts have not found it necessary to devote a greater portion of their deliberation to the determination of controversies over the respective liabilities of parties thereto involved. Perhaps, the reasons for the relatively insignificant amount of litigation involving the liability of parties to checks may be attributed to the fact that in the past several years there have been few bank failures, and no little credit should be given to the drafters of the Uniform Negotiable Instruments Act for the clarity of the sections of the act applicable to checks. The scope of the following material will be limited to the probing of problems relating to the time allowed a holder of a check in which to make presentment for payment in order to establish the liability of the drawer and indorsers thereto.

Daniel in his work on Negotiable Instruments defines a check as: "A draft or order upon a bank or banking house, purporting to be drawn upon a deposit of funds, for the payment at all events of a certain sum of money to a certain person therein named, or to his order or bearer, and payable instantly on demand."[7] A check is similarily defined by section 185 of the Uniform Negotiable Instrument Act[8] as: ". . . A bill of exchange drawn on a bank payable on demand." The act further provides "except as herein otherwise provided, the provisions of this chapter applicable to a bill of exchange payable on demand apply to a check."

It is important in determining the rights of the respective parties to point to the distinctions between an ordinary bill of exchange and a check. By definition a check must be drawn upon a bank,[9] while a bill of exchange need not have a bank as the named drawee. A check need not be accepted as it only calls for payment upon timely presentment.[10] The execution of a check contemplates that the drawer has sufficient funds on deposit with the drawee to provide for the payment of the check when it is presented for payment.[11] Unlike the drawer of a bill of exchange, the drawer of a check is not relieved of liability by the failure of the holder to have made timely presentment for payment but, as will be later discussed, the drawer of a check is in such case relieved of liability to the amount of damages that he may show that resulted from the unexcused delay in making presentment of the check for payment.[12] A check is not due until payment has been demanded, the statute of limitations would then only begin to run.

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[7] Daniel on Negotiable Instruments, 7th ed., vol. 3, p. 1791, § 1748 (1933); for other but similar definitions of a check see: Rogers v. Durant, 140 U.S. 298, (1891); Industrial Bank v. Bowes, 165 Ill. 70, 75, 46 N.E.10, 12 (1897).

[8] Hawley v. Jette, 10 Ore. 31 (1881); Gifford v. Hardell, 81 Wis. 538, 60 N.W. 1024 (1894).

It is not at all uncommon for one to deliver his draft drawn upon a bank to postdate the instrument. Is such an instrument, which we commonly refer to as a postdated check, in reality a check or is it a bill of exchange? Is such an instrument payable on demand when the holder is required to refrain from presenting the document for payment until the date of the instrument? In *Champion v. Gordon,*[13] Judge Sharwood said in answer to these questions: "It is not denied that a postdated check cannot be presented for acceptance. That is by implication payable on a future date. . . . It is a check and not a bill of exchange. More than twenty years ago banks of Philadelphia under the advice of counsel adopted this rule, and it has been their uniform practice ever since. The usage of the banks in the commercial metropolis of the state ought to have great weight in determining a question of this character. It is perhaps quite as important that such usage should not be disturbed, as that the point should be decided abstractly or theoretically right." Obviously a postdated check, unlike a time bill of exchange, cannot be dishonored before its actual date.[14] In holding such instrument to be a demand instrument, presentment for payment need not be made on the exact date of the postdated check as a condition to the establishment of the liabilities of the drawer and indorsers. Presentment within a reasonable time after its date is sufficient to charge the drawer.[15] The fact that the check is postdated does not affect its negotiable character.[16]

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[9] Minot v. Russ, 156 Mass. 458, 31 N.E. 489 (1892).

[10] Gifford v. Hardell, 88 Wis. 538, 60 N.W. 1064 (1894).

[11] UNIFORM NEGOTIABLE INSTRUMENTS ACT, § 186; Exchange Bank v. Sutton Bank, 78 Md. 577, 28 Atl. 563 (1894).

[12] 70 Pa. 474, 476 (1872).

[13] Wilson v. McEachern, 9 Ga. App. 584, 71 S.E. 946 (1911).

Where, however, the instrument which purports to be a check shows on its face that it was drawn on one date and to be due at some subsequent designated date, the cases are in conflict whether one is then dealing with a check or a bill of exchange. The better reasoned cases have held such instruments to be bills of exchange, as distinguished from checks.[17] These cases dealt with days of grace which were formerly allowed on a bill of exchange, but which were not permitted in the case of a check. As the days of grace have been abolished by section 85 of the Uniform Negotiable Instruments Act[18] these cases lose much of their significance. The determination as to whether such an instrument be a check or a bill of exchange is still important in determining whether the drawer is released of liability as the result of the holder failing to make proper presentment thereof for payment. In the absence of showing of due presentment for payment the drawer of a bill of exchange is released of liability, while the drawer of a check would only be released to the amount of damages suffered by reason of the delay in making a timely demand of the drawee for payment.

In order for the holder to perfect his rights as a condition precedent to suit against the drawer or indorsers on a *bill of exchange* on their secondary liability, it is necessary for the holder to allege and prove that he had made proper presentment of the bill for acceptance or payment, or acceptance and payment, and to have had the instrument dishonored by nonacceptance or nonpayment, followed by timely notice of the dishonor. Otherwise the holder will be denied the right to seek payment of the instrument from the drawer or indorsers.[19]

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[14] Philadelphia Life Ins. Co. v. Hayworth, 296 Fed. 339 (4th Cir. 1924).

[15] UNIFORM NEGOTIABLE INSTRUMENTS ACT, § 12; Triphonoff v. Sweeney, 65 Ore. 299, 130 Pac. 979 (1913).

[16] In the case of Harrison v. Nicollet Nat. Bank, 41 Minn. 488, 43 N.W. 336 (1889) a draft for money drawn on a bank, payable at a day subsequent to its date, and subsequent to the date of its issue was held not to be a "check", but a bill of exchange. While in Way v. Towle, 155 Mass. 374, 29 N.E. 506 (1898) an instrument in the form of a check which was dated August 31, 1899, ordering bank to pay on October 1, 1899, was treated as a check and not as a bill of exchange.

[17] "Every negotiable instrument is payable at the time fixed therein without grace . . . ."

[18] UNIFORM NEGOTIABLE INSTRUMENTS ACT, §§ 61, 66, 72, 73.

The failure of the holder of a *check* to establish that the check was properly presented for payment and due notice of dishonor was given will bar the holder from proceeding against the indorsers on the basis of their secondary liability as set forth in section 66 of the Uniform Negotiable Instruments Act.[20] In comparison with the liability of the drawer of a bill of exchange, other than a check, the failure of the holder to prove that the check was timely presented for payment will not discharge the drawer of the check completely of liability, but will release him of liability only to the extent that the drawer has incurred a loss by reason of such delay in presenting the check to the drawee for payment.[21] If the drawer has suffered no loss or damage by reason of the delay in making presentment for payment, as where he had no funds on deposit with the drawee to cover the check,[22] or where the drawer had previously ordered the bank to stop payment,[23] he has no cause to complain of the holder's delay in demanding payment from the drawee and his liability is therefore not affected.

When the drawee bank has ceased to operate in the interval between the time of issuance of the check and the date payment was demanded from the bank, upon showing undue delay in making presentation of the check for payment, and that the check would have been paid by the drawee had it been timely presented, a presumption arises that the drawee has suffered damages by reason of the delay in making presentment for payment and casts on the holder the burden of otherwise showing.[24] For example, if the check from A to B drawn upon C bank in the sum of $100 is held an unreasonable time after issue before it was presented for payment and the bank had during this interval ceased to operate, and the bank subsequently returns to the drawer only forty cents on each dollar which was on deposit at the time the bank closed its doors, the drawer has been damaged to the extent of sixty cents on each dollar by the holder's failure to have timely presented it for payment. The holder of the check is thus only entitled to recover $40 from the drawer, and must suffer the balance of the loss himself, unless he should have the right to collect from a prior indorser.

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[19] An indorser is discharged by unreasonable delay in presentation of a check though he suffered no loss therefrom. Swift v. Miller, 62 Ind. App. 312, 113 N.E. 447 (1916); Nuzum v. Sheppard, 87 W. Va. 243, 104 S.E. 487 (1920); Cominsky v. Kleiner, 34 Misc. 181, 68 N.Y.S. 776 (Supreme Ct. 1901); In an action by bank to recover from indorser whom it had credited with the amount of the check and had permitted to withdraw the money, the burden is on the bank to show a presentation of the check to the drawee within a reasonable time. Knickerbocker Trust Co. v. Miller, 149 App. Div. 685, 133 N.Y. Sup. 989 (Supreme Ct. 1912); Millet v. Miller, 135 Neb. 123, 280 N.W. 123 (1938).

[20] Nuzum v. Sheppard, 87 W. Va. 243, 104 S.E. 587 (1920).

[21] Gilman v. F. O. Bailey Carriage Co., 127 Me. 91, 141 Atl. 321 (1928); note 24 Mich. L. Rev. 498 (1925); Uniform Negotiable Instruments Act, § 79.

[22] Uniform Negotiable Instruments Act, 79; Sebree v. Thomas, 166 Ill. App. 427 (1911); Usher v. A. I. Tucker Co., 217 Mass. 441, 105 N.E. 360 (1914).

[23] Watt v. Gans, 114 Ala. 264, 21 So. 1011 (1897); Stevens v. Park, 73 Ill. 387 (1874); The presumption of loss arising out of want of diligence in presentation of a check, and the intervening failure of the drawee, may be rebutted by proof that the drawee had no funds with the drawer to meet the check, or that he had withdrawn them before the bank failure.

When the drawer is released of liability on the check under the above facts, he is similarly released of liability on the underlying debt. That is, the creditor drawer if sued on the debt instead of as drawer, may plead payment of the underlying debt.[25] As goes the drawer's liability on the check, so goes the liability on the underlying debt.

In considering the period of time allowed the holder of a check to make due presentment for payment in order to fix the drawer's liability, see section 186 of the Uniform Negotiable Instruments Act. This section provides: "A check must be presented for payment within a reasonable time after its issue or the drawer will be discharged from liability thereon to the extent of the loss caused by the delay."[26] This section by its language only applies to the liability of the drawer and makes no reference to that of an indorser.

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[24] In Kirkpatrick v. Association, 119 Pa. St. 20, 12 Atl. 754, 755 (1888) Judge Sterrett said: "It is well settled that, in the absence of an agreement to the contrary, a check or promissory note, of either the debtor or a third person, received for a debt, is merely conditional payment,—that is, satisfaction of the debt if and when paid,—but the acceptance of such note or check implies an undertaking of due diligence in presenting it for payment, etc., and, if the party from which it is received sustains loss by want of due diligence, it will be held to operate as actual payment." In cases where the creditor has given his own check in payment of his indebtedness, the burden is upon the drawer to show both delay and loss. Such holding puts the burden upon him, not only to show delay in presentment, but loss to himself in consequence. Kahn v. Walton, 46 Ohio St. 195, 20 N.E. 203 (Michie 1955).

[25] Maryland Casualty Co. v. Dobin, 108 S.W.2d 166 (Mo. App. 1937).

In the determination of what is a "reasonable" or an "unreasonable time" in which to present the check for payment, consideration must be given to the nature of the instrument, any usage of trade and business with respect to such instruments, and the facts of the particular case.[27] As a check is not intended to be in circulation as a substitute for money, a reasonable time in this situation will necessarily be a relatively short period. Ordinarily when the check is drawn and is to be paid in the same town it should be presented to the drawee for payment on the day of its receipt or the next business day.[28] When, however, a check is received at a distant place it must be forwarded by the next secular day by some recognized method of transmission to some person or agency at the place of payment, who has until the next secular day to make presentment for payment.[29] It has been held that failure to forward a check for collection on the next business day is negligence where the bank is in another place.[30]

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[26] Lowell Co-operative Bank v. Sheridan, 284 Mass. 594, 188 N.E. 636 (1934); Reasonable time for presentment of a check on drawee in same place includes only banking hours of next business day after delivery. Maryland Title Guarantee Co. v. Alter, 167 Md. 244, 173 Atl. 200 (1934).

[27] Seager v. Dauphinee, 284 Mass. 96, 187 N.E. 94 (1933); Nuzum v. Sheppard, 87 W. Va. 243, 104 S.E. 587 (1920).

[28] Nuzum v. Sheppard, 87 W. Va. 243, 104 S.E. 587 (1920). In Jett Bros. Stores v. McCullough, 188 Ark. 1108, 69 S.W.2d 863 (1934) the payee deposited check in home town bank two days after receipt, but only one banking day having intervened, the check being presented to the drawee in due course, held no unreasonable delay.

Three days' delay in presenting check for payment held not unreasonble where payee a school teacher had been engaged in teaching school on each of those days. Peterson v. School District, 162 Minn. 347, 203 N.W. 46 (1925). Three days delay in presentment of check for payment, held unreasonable delay where payee was cautioned by drawer that drawee bank was in precarious condition. Sinclair Refining Co. v. Keitch, 97 Okla. 55, 221 Pac. 1003 (1924).

Unexplained delay of four days in presenting check for payment held unreasonable. J. S. Martin Lumber Co. v. Rice, 133 Okla. 162, 276 Pac. 744 (1929). One engaged in farming lived eight miles from town received a check on Tuesday failed to present check for payment until Saturday, held, not guilty of unreasonable delay so as to lose his rights against drawer where the bank failed, especially in view of the fact that the farmer had very little business training and seldom went to town except on Saturday. Barry v. Harris, 186 Ark. 481, 54 S.W.2d 289 (1932).

Five days unreasonable delay. Seager v. Dauphinee, 284 Mass. 96, 187 N.E. 94 (1933); Seven days delay and thirteen days delay in making presentment held unreasonable delay in Swift v. Miller, 62 Ind. App. 312, 113 N.E. 447 (1916), and Plainsville v. Rooks County, 137 Kan. 61, 19 P.2d. 911 (1933) respectively.

[29] Krauss v. Aleck, 202 Iowa 91, 209 N.W. 444 (1926); Grant City First National Bank v. Korn, Mo. App. 179 S.W. 721 (1915); Nuzum v. Sheppard, 87 W. Va. 243,

Whether or not in a given undisputed factual situation due diligence has been exercised in making presentment is a question of law to be determined by the court.[31] Where the facts are in dispute and are capable of sustaining more than one conclusion, the question of reasonableness is for the jury.[32]

AS TO INDORSERS

Section 185 of the Uniform Negotiable Instrument Act states: "Except as herein otherwise provided, the provisions of this act applicable to a bill of exchange payable on demand apply to a check."[33] As the act does not otherwise distinguish the liability of an indorser of a check from an indorser of a bill of exchange, it must therefore be taken that the liability of an indorser on either type of instrument will be the same.

One must examine section 66 of the Uniform Negotiable Instruments Act[34] to determine the liability of an unqualified indorser on either a check or a bill of exchange. The last paragraph of this section fixes the conditional liability of an indorser by stating: ". . . And, in addition, he engages that on due presentment, it shall be accepted or paid, or both, as the case may be, according to its tenor, and that if it be dishonored, and the necessary proceedings on dishonor be duly taken, he will pay the amount thereof to the holder, or to any subsequent indorser who may be compelled to pay it." In the case of an indorser of a check we are only concerned with due presentment for payment, as a check may not be presented for acceptance as might a time bill of exchange.

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104 S.E. 587 (1920). Contra: In Citizens' Bank v. Pleasantville First Nat. Bank, 135 Iowa 605, 113 N.W. 481 (1907) the court stated that it is not the universal rule that even if the facts are not in dispute the question whether the presentment was within a reasonable time is for the court.

[30] Empire-Arizona Copper Co. v. Shaw, 20 Ariz. 471, 181 Pac. 464 (1919); Slaymen v. Welch First National Bank, 104 W. Va. 265, 139 S.E. 750 (1927).

[31] Britton on Bills and Notes, p. 867 (1943).

[32] 134 Wis. 218, 114 N.W. 451, (1908); Plover Savings Bank v. Moodie, 135 Iowa 685, 110 N.W. 29, 110 N.W. 476 (1907).

[33] Norton, Bills and Notes 4th Ed. note 2, p. 500 (1914).

[34] Dougherty v. Shankland, 217 Ia. 951, 251 N.W. 73 (1933).

The real issue and problems relating to indorser's liability springs from the unclear language of section 71 of the Uniform Negotiable Instruments Act which states: ". . . Where it is payable on demand, presentment must be made within a reasonable time after its issue, except that in the case of a bill of exchange, presentment for payment will be sufficient if made within a reasonable time after the last negotiation thereof."[35] The holder of a check is given the same period of time in which to make presentment for payment as the holder of a bill of exchange is allotted in which to make presentment in order to establish the liability of the drawer or indorsers thereon. The reasonable time for presentment in order to fix the liability of an indorser of a bill of exchange or a check is measured from the last negotiation, while the reasonable time in the case of the drawer of a check or bill of exchange is measured from the issuance of the instrument. The yardstick of time is the same length in either of the cases, but the date from which the measurement starts presents some most troublesome problems.

The question might be asked, can the liability of the indorser on a check be preserved indefinitely, so long as each negotiation follows promptly after each indorser acquired title to the instrument? Mr. Britton in his work on *Bills and Notes* in partial answer to this question stated: "[I]f an indorsee holds the instrument for such a period of time that a negotiation by him would not be within a reasonable time after the last negotiation, it would seem that the liability of the antecedent secondary parties would be discharged as to him. The question as to whether the liability of such parties would be revived as regards an indorsee who acquired title after the lapse of a reasonable time from the immediately preceding negotiation and as regards subsequent holders would turn on the question whether such holders were holders in due course."[36]

In referring to the last paragraph of section 66 of the Uniform

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[35] Smith v. Miller, 43 N.Y. 171 (1870).

[36] Smith v. Janes, 20 Wend. 192, 32 Am. Dec. 527 (N.Y. 1838). A check was not presented for nine days after receipt by the plaintiff. The indorser was held discharged irrespective of any question of loss. Proper presentment was a condition precedent to indorsers liability, and his delay was not excused even when the drawer was without funds on deposit, or because presentment would have been unavailing as a means of procuring payment.

Negotiable Instruments Act,[37] it will be noted that the secondary liability of an indorser was said to extend to subsequent *holders* of the instrument. Does the liability of the indorser really extend to subsequent holders who are unable to qualify as holders in due course? The first paragraph of this section dealing with the warranties of an indorser indicates that such liability of an indorser for breach of warranty extends to subsequent *holders in due course*. It was surely not the intention of the drafters of the act to limit the liability of an indorser for breach of warranty to a holder in due course and permit the indorser's conditional liability to extend to one who is only a holder of the instrument. It seems more logical and desirable to hold that the term holder in due course as used in the first portion of section 66 should be interpreted as to include holders as well. This would extend the liability of an indorser on both the warranties and conditional liabilities to the same persons. No logical reason can be given for the difference in the language.

Quoting from section 53 of the Uniform Negotiable Instruments Act: "Where an instrument is payable on demand is negotiated an unreasonable length of time after its issue, the holder is not deemed a holder in due course. It is suggested that close examination of sections 53, 66, and 71 of the act will show that it is possible for one who is unable to qualify as a holder in due course, (*i.e.*, having acquired the instrument an unreasonable time after issue) to find that he has nevertheless acquired the instrument within a reasonable time after the last negotiation, and therefore be entitled to proceed against prior indorsers on their conditional liability as set forth in section 66.

At least three important factual situations arises regarding the time allowed a holder in which to make timely presentment of a check or bill for payment in order to fix the indorser's liability thereon: first, where the check has been held an unreasonable length of time by the holder before making presentment for payment; secondly, where the check has been outstanding an unreasonable period before the first negotiation, the holder presents the check for payment within a reasonable time after acquiring the check; thirdly, the bill or check indorsed and delivered by several successive indorsers, the last of which was beyond a reasonable time after issue, the holder making demand of the drawee for payment within a reasonable time after its receipt.

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[37] Comer v. Dufour, 95 Ga. 376, 22 S.E. 543 (1895).

In *Columbian Baking Co. v. Brown* involving a draft sold by a bank to defendant on June 10, indorsed and mailed to T on June 16, who received it on June 20, on July 14 sold it to plaintiff bank, which in turn sent it to a Chicago bank which presented it for payment on July 18, it then being dishonored. In a suit by the plaintiff bank against an indorser, recovery was allowed. The court stated "A bill of exchange payable on demand, regardless of its character, put in circulation, so long as its circulating character is preserved may be outstanding without impairing the liability of indorsers thereon . . . only the time need be considered intervening between the last negotiation and the presentment." This language was clearly dicta since the court found that under the facts of the case an unreasonable time had not elapsed from the time of issue till time payment was demanded and denied.

After considering the several sections of the Uniform Negotiable Instruments Act and the dicta in the *Columbian Baking Co.* case, the following solutions to the three factual problems may be justified. As to the first, where the check was held an unreasonable time by the holder before making presentment, such holder would have the right to look to the drawer for payment to the extent that the drawer had not been damaged by the delay in demanding payment. As the holder had failed to present the check within a reasonable time after having received it, the holder would be denied the right to look to prior indorsers for payment.

In the second illustration, the check having been outstanding more than a reasonable time after issue before the first negotiation, we would not be concerned with a holder in due course being involved. Under the language of section 71 of the Uniform Negotiable Instruments Act and the dicta in the *Columbian Baking Company* case, any prior indorser could be reached on the basis of his conditional liability, as the holder could show presentment for payment had been made within a reasonable time after the last negotiation. The holder would find himself as to his rights against the drawer to be the same as in the above problems. In the third situation, certainly the last indorser should be held liable to the holder upon showing that presentment for payment was made promptly after the holder took the bill or check and followed with necessary proceedings of dishonor. As to the holder's rights against prior indorsers, the answer is not nearly so simple. Does each indorser only agree to be liable to a holder who makes presentment for payment promptly after his negotiation? That is, may the indorser be relieved of liability by the passage of a reasonable time and then have his liability revived by a new negotiation followed by immediate presentment for payment and due notice of dishonor? It is suggested that in answer to these questions it is possible for an indorser to find himself relieved of liability by showing that the check or bill had been held an unreasonable time by some holder, but discovery that his liability was revived by another negotiation followed by timely presentment and necessary steps of dishonor.

Some of the confusion and uncertainty regarding the rights of the holder in proceeding against indorsers on checks would be simplified if we were to follow the suggestion of Mr. Norton in his works on negotiable instruments when he said: " . . .[I]t would seem reasonable to construe section 71 of the act as laying down a rule applicable only to the liability of the indorser who was a party to the last negotiation, or as declaring the rule that presentment must be made within a reasonable time after the negotiation of the instrument by the person sought to be charged. . . . So construed, the statute declares the former rule of the law merchant as stated in the English Bills of Exchange Act. . . ."

As the indorser's contract is separate and distinct from that of any other persons to the instrument[41] the indorser's obligation to pay does not accrue until after due presentment, and necessary proceedings of dishonor have been duly taken, the statute of limitations as to his liability would then only begin to run. It is not necessary that the holder exhaust his remedies against the drawer before proceeding against an indorser of a check.

Where the check of another is indorsed by the debtor in payment of his debt, the holder's failure to properly present such check and demand payment promptly will release the debtor as to his liability as an indorser and likewise as to his liability on the original indebtedness for which the check was negotiated[42] irrespective of any loss or damage to the indorser.[43] Inquiry as to whether the indorser was or was not injured by the delay in failing to present the check for payment is immaterial as his release is based on failure to properly present the instrument and not on the basis of damages thereby suffered.

1958 Developments in the Law—Banks and Commercial Paper

JAMES S. SAVAGE

Banks and Banking.—Most of the cases in the area of banks and banking dealt with rather routine matters. The decision of the New York Court of Appeals in *Miller v. Discount Factors, Inc.*,[135] forbidding business corporations from making "discounts" and engaging in other banking activities, focused attention on the permissive limits of the Banking Law, and occasioned further decisions by New York courts. The Supreme Court, Appellate Term, First Department, held that the lending of money on security of chattel mortgages did not violate the law.[136] The same court, at special term in New York County, ruled that discounting in violation of the law against unauthorized banking would be a defense against any attempt to enforce the note, and that the invalidity could be used as a defense, even on an action for money loaned.[137] The Court of Appeals held that even if notes were invalid under the Banking Law, this would not effect the mortgage given as security for the notes.[138] The supreme court, at trial term in Kings County, held that the exception in the statutes, allowing a corporation other than a bank to discount notes, applies only to corporations in the business of loaning money secured by mortgages on personal property affixed to land; the statute does not except corporations loaning money secured by mortgages on automobiles.[139]

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[135] 1 N.Y.2d 275, 135 N.E.2d 33, 152 N.Y.S.2d 273 (1956).

[136] Shorenstein v. Karmiol, 10 Misc. 2d 947, 170 N.Y.S.2d 111 (Sup. Ct. 1957).

[137] Feuchtwanger Corp. v. South Am. Commodities, Inc., 9 Misc. 2d 624, 173 N.Y.S.2d 390 (Sup. Ct. 1957).

[138] Amherst Factors, Inc. v. Kochenburger, 4 N.Y.2d 203, 149 N.E.2d 863, 173 N.Y.S.2d 570 (1958).

[139] Flatbush Auto Discount Corp. v. McCarthy-Bernhardt Buick, Inc., 3 Misc. 2d 850, 177 N.Y.S.2d 269 (Sup. Ct. 1958).

One of the most unusual cases of 1955 involved the conviction of a depositor in a national bank for aiding, abetting, and inducing a cashier to misapply bank funds.[140] The United States Court of Appeals for the Sixth Circuit affirmed this past year, with one judge dissenting.[141] Over a period of several years, the cashier of a bank in Kentucky had caused the bank to honor checks without charging them against the accounts of various depositors. His reason for doing this was that, during most of this period, these depositors, 135 in all, were overdrawn. The total of the uncharged checks amounted to a figure slightly in excess of $500,000. The convicted depositor was overdrawn, at the time of discovery, in the amount of $74,000, and his almost wholly-owned corporation in the amount of $150,000. There was evidence that the depositor knew that when his, or his corporation's, checks arrived at the bank, they would be honored. The majority of the court held that:

> If he had such knowledge and continued over a course of years to engage in a course of conduct which so misapplied the funds of the bank and which required the expected collaboration of the cashier to make it successful, we think the evidence was sufficient to take the case to the jury on the issue of aiding, abetting, or inducing.[142]

Circuit Judge Stewart, in his dissenting opinion,[143] felt that it was not enough to show that the depositor had created the occasion or the opportunity for misapplication, even though such consequence may have been foreseen. He asserted that aiding and abetting "involves much more than merely 'causing an act to be done.' "[144]

In Pennsylvania, a depositor in a bank and an executive of the bank were engaged in a kiting operation that lasted for twenty-three months, and involved over a million dollars. The bank executive committed suicide, but just before he did so he took two checks of the depositor, which had been signed in blank, and filled them in for a total of $19,000, making them

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[140] United States v. Logsdon, 132 F. Supp. 3 (W.D. Ky. 1955).
[141] Logsdon v. United States, 253 F.2d 12 (6th Cir. 1958).
[142] Id. at 15.
[143] Id. at 16.
[144] Ibid.

payable to the bank. It was discovered, immediately after t
suicide, that the bank was insolvent, and it was closed. T
depositor brought an action aganist the Federal Deposit I
surance Corporation in the United States district court to r
cover for the checks, on the ground that the executive of t
bank had filled the checks out without the depositor's authori
and that the checks had nothing to do with the kiting operatio
The jury granted him the verdict, but the trial court gave jud
ment *non obstante veredicto* and, alternatively, granted a m
tion for a new trial.[145] The United States Court of Appeals f
the Third Circuit affirmed the judgment *non obstante vered*
to.[146] Noting that a course of conduct once established is pr
sumed to continue, the court held that the depositor had fail
to show that the use of these two checks was not a part of t
entire kiting operation.[147] These cases reflect some weakness
in the examination of banks by both federal and state agenci

The New Hampshire Supreme Court held that it was neg
gence for a bank to pay its own money order, payable to
named corporation, on the endorsement of the corporatio
name by its local office manager, without determining his a
thority.[148] The manager appropriated the money to his own us
and the corporation's surety was allowed to recover agai
the bank, the court rejecting the argument that the loss w
caused by the unauthorized use of the proceeds by the manag
The court held that the payment of the money to the manag
created the opportunity for misappropriation.[149]

Commercial Paper.—The number of cases involving co
mercial paper in 1958 was about the same as in the previo
year. The "home improvement loan" cases, which have be
giving difficulty since the end of World War II, seem to ha
dropped off some during 1958. These cases all follow pret
much the same pattern. A contractor undertakes to moderni
or improve a home, and induces the householder to sign

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[145] Falconi v. Federal Deposit Ins. Corp., 153 F. Supp. 867 (W.D. Pa. 1957).

[146] Falconi v. Federal Deposit Ins. Corp., 257 F.2d 287 (3d Cir. 1958).

[147] Id. at 291.

[148] Security Fence Co. v. Manchester Fed. Sav. & Loan Ass'n, 101 N.H. 190, 1
A.2d 910 (1957).

[149] Id. at 913.

contract that carries with it a promissory obligation. He sells the obligation to a financing institution, and then either defaults on the contract, or does not perform as promised. The householder is unwilling to pay, and a lawsuit customarily follows. Four such cases (though one involved the construction of a new house) were decided during the year. The United States district court in Wisconsin decided, in a case of this sort, that the United States had not met the burden of proving itself a holder in due course.[150] In a similar case in New York,[151] the householder alleged, in a general denial of the assignee's claim, that the assignee had full knowledge of the contract, and the conditions under which the note was given, at the time that it took its assignment. The court held that this denial raised a triable issue with regard to due course holding, and precluded entry of summary judgment. In a Pennsylvania case,[152] the notes were nonnegotiable, but the householder had signed completion certificates stating that the work had been satisfactorily completed, and this before the assignment of the notes to a bank. The Pennsylvania court held that the householder was estopped from asserting a failure of consideration. In an Ohio case,[153] a lower court held that the financing agency, under the circumstances of the case, should be regarded as the real payee of the notes, rather than the transferee, and that, as the real payee, the defense of failure of consideration would be available to the maker.

The United States lost some money on a deputy tax collector who turned in some fictitious income tax returns showing a refund owing from the Government. Without any further investigation, checks for these refunds were issued, the collector secured possession of them, indorsed them in the name of the fictitious payees, and cashed them in various banks. All of the banks handling the checks were required to guarantee prior indorsements before presenting them to the Federal Reserve for payment. After the loss was discovered, the government

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[150] United States v. Schumacher, 154 F.Supp. 425 (E.D. Wis. 1957).

[151] Stratford Credit Corp. v. Pettrone, 11 Misc. 2d 65, 177 N.Y.S.2d 994 (County Ct. 1958).

[152] United States Nat'l Bank v. Drabish, 144 A.2d 640 (Pa. Super. Ct. 1958).

[153] Botzum Bros. Co. v. Brown Lumber Co., 104 Ohio App. 507, 150 N.E.2d 485 (1957).

brought an action against these presenting banks on the
guarantees. The district court held for the Government, ar
the banks appealed. The Court of Appeals for the Fifth Ci
cuit reversed, one judge dissenting, holding that under tl
"fictitious payee" rule the indorsements were not forgeries, ar
the banks would not be liable on their guarantees.[154] Tl
court held that the loss to the Government was occasioned l
the acts of a dishonest employee, and that "the necessity f
unfettered circulation of the Government's negotiable pap
not only does not require—it actually forbids—that such lo
should be visited on the collecting banks."[155]

In another "fictitious payee" case, the Florida Supren
Court reversed a summary judgment against the drawee, in a
action against it by the drawer to restore the amount of tl
check, and remanded to allow the drawee an opportunity eith
to show that the payee was fictitious, or that the intended pay
actually received the money.[156] The United States Court
Appeals for the District of Columbia in a similar case reache
the same result.[157] In two cases that arose in 1958, husban
forged their wives' names to promissory notes. In one case, tl
payee allowed the maker, after the co-maker's signature ha
been affixed, to take the note out of the payee's office to secu
the signature of the maker's wife. The maker forged his wife
signature, and returned the note. Held: the payee could n
recover from the co-maker.[158] In the other case, the pay
issued a check to husband and wife on the basis of a contra
and note, on both of which the husband had forged the wife
signature. The husband forged his wife's indorsement on tl
check, and the payee, unable to collect upon the contract ar
note, brought an action against its bank to restore the amou
of the check. Held: since the proceeds of the check went

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[154] Atlantic Nat'l Bank v. United States, 250 F.2d 114 (5th Cir. 1957). See al
Notes, 58 Colum. L. Rev. 899 (1958), 27 Fordham L. Rev. 135 (1958), 32 Tul.
Rev. 755 (1958).

[155] Atlantic Nat'l Bank v. United States, supra note 154, at 118.

[156] Florida Nat'l Bank v. Geer, 96 So. 2d 409 (Fla. 1957). See also McKen
Negotiable Instruments, 12 U. Miami L. Rev. 464, 467 (1958); 4 How. L.J. 1
(1958); 32 Tul. L. Rev. 133 (1957).

[157] Rubinstein v. Goldkind, 255 F.2d 530 (D.C. Cir. 1958).

[158] Public Loan Corp. v. Jacobs, 144 N.E.2d 505 (Ohio App. 1955).

the very person intended, the husband, there could be no recovery against the bank.[159]

Among other decisions in the area of commercial paper, for the most part routine applications of settled law, courts reiterated the principle that there is a limit to the time in which a depositor can wait after receiving his statement and cancelled checks, and still claim restoration of funds paid out on checks with forged indorsements;[160] that the giving of an immediate, unrestricted credit to a depositor on checks deposited by him constitutes value sufficient to make the bank a holder in due course;[161] and that a signature placed on an instrument by carbon paper would keep it from being a negotiable instrument.[162] Finally, the usual large number of cases were decided entirely on the determination that the holder was in due course,[163] or that he was not.[164]

Usury.—There were thirty some appellate cases decided in 1958 in which usury, either raised as a defense to an action on a note or contract, or used as the basis for a recovery by a maker, was the principal issue. Because of local variances in usury statutes, many of the cases are only of local interest. In addition, many cases in which usury was raised were finally determined on the basis of factual inquiries, or routine applications of law, such as how much interest had actually been charged,[165] on whether an alleged "broker's commission" was really that;[166] on the effect of a commission paid to the same person to whom interest is to be paid;[167] on whether an accommodation indorser is in sufficient privity to recover usurious interest;[168] and on whether it is usurious for the assignee of a conditional sales contract not to grant a refund credit for the time-price differential to a buyer who is in default.[169]

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[159] Commercial Credit Corp. v. Empire Trust Co., 156 F. Supp. 599 (W.D. Mo. 1957), 56 Mich. L. Rev. 1188 (1958).

[160] Gerber v. Continental Ill. Nat'l Bank & Trust Co., 16 Ill. App. 2d 379, 148 N.E.2d 597 (1958); Housing Authority v. Commonwealth Trust Co., 25 N.J. 330, 136 A.2d 401 (1957); Peppas v. Marshall & Isley Bank, 2 Wis. 2d 144, 86 N.W.2d 27 (1957).

[161] Universal C.I.T. Credit Corp. v. Guaranty Bank & Trust Co., 161 F. Supp. 790 (D. Mass. 1958); Meadow Brook Nat'l Bank v. Paramount Factors, Inc., 8 Misc. 2d 362, 167 N.Y.S.2d 468 (Sup. Ct. 1957).

[162] Chrismer v. Chrismer, 103 Ohio App. 23, 144 N.E.2d 494 (1956), 9 W. Res. L. Rev. 349 (1958).

[163] E.g., Security Fin. Co., v. Kone, 307 S.W.2d 163 (Tex. Civ. App. 1957).

[164] E.g., Dakota Transfer & Storage Co. v. Merchants Nat'l Bank & Trust Co., 86 N.W.2d 639 (N.D. 1957).

[165] Ables v. Curle, 102 So. 2d 122 (Miss. 1958).

[166] Wheeler v. Superior Mortgage Co., 325 P.2d 156 (Cal. App. 1958).

[167] Industrial Bank v. Page, 249 F.2d 938 (D.C. Cir. 1957).

It was long thought that conditional sales contracts should not come under usury statutes.[170] The usual qualification of a bona fide "sale" has always been a part of this approach. Recently, a number of state courts have started bringing bona fide conditional sales under the usury statutes. In 1957, the Nebraska Supreme Court joined in the procession.[171] In 1958, the same court was presented with two cases which, on the surface, appeared to be normal time-price sales, and thus valid within Nebraska law. In both cases the court, after reviewing the evidence, concluded that there was not a good faith time-price sale.[172] The same court also held (with a dissent) that a sheriff who attached a trailer for the benefit of general creditors could not raise the defense of usury in a replevin action brought by the chattel mortgagee.[173]

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[168] Lydick v. Stamps, 316 S.W.2d 107 (Tex. Civ. App. 1958). See Jones, Usury Laws and Enforcement in Texas, 36 Texas L. Rev. 606 (1958).

[169] Imperial Thrift & Loan v. Ferguson, 155 Cal. App. 2d 866, 318 P.2d 566 (1957).

[170] Note, 71 Harv. L. Rev. 1143 (1958).

[171] McNish v. Grand Island Fin. Co., 164 Neb. 543, 83 N.W.2d 13 (1957).

[172] Curtis v. Securities Acceptance Corp., 166 Neb. 815, 91 N.W.2d 19 (1958); Nelson v. General Credit Corp., 166 Neb. 770, 90 N.W.2d 799 (1958).

[173] Commonwealth Trailer Sales v. Bradt, 166 Neb. 1, 87 N.W.2d 705 (1958).

BANKING DECISIONS

In this department are published each month all of the important decisions of the Federal and State Courts involving questions pertaining to the law of banking and negotiable instruments. The experiences they disclose deserve careful attention and study of bankers, bank counsel, the depositor and the bank student seeking advancement.

Repayment of Loan to Bank Ruled Not to Be Voidable Transfer

Under the Bankruptcy Act the following provision bears on the subject of voidable transfers:

> "Every transfer made and every obligation incurred by a debtor within one year prior to the filing of a petition initiating a proceeding under this title by or against him is fraudulent . . . (b) as to the then existing creditors and as to the other persons who become creditors during the continuance of a business or transaction, if made or incurred without fair consideration by a debtor who is engaged or is about to engage in such business or transaction, for which the property remaining in his hands is an unreasonably small capital, without regard to this actual intent: . . ." § 67, sub. d (2) (b), 11 U.S.C.A. § 107, sub. d (2) (b).

In a rather lengthy opinion a federal district court has interpreted this portion of the Act and has ruled that the repayment of a twelve day loan to a bank by a borrower who became bankrupt within a year did not constitute a voidable transfer as contemplated in the Act.

The loan had been made by the bank to one of its established customers who requested the loan for a company he was reactivating. Twelve days after the loan was made the customer repaid it on the basis that the purpose for which the loan was made could not be carried out. Within a year the customer became bankrupt and it appeared that he had probably been in financial difficulty when borrowing the funds. The court ruled essentially that when the represented purpose of the loan failed the bank had the right to demand repayment

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NOTE—For similar decisions see B. L. J. Digest (Fifth Edition) **§ 145.**

under Louisiana law. Because this right existed the transfer of the funds back to the bank was not a transfer "without fair consideration" and thus the transfer was not voidable under the Act. *W. T. Mayo v. Pioneer Bank & Trust Company*, United States District Court, W.D. Louisiana, 168 F. Supp. 503. The opinion of the court is as follows:

Findings of Fact and Conclusions of Law

BENJAMIN C. DAWKINS, Jr., C.J.—This cause having been submitted for decision, by the Court without a jury, the Court having considered the pleadings, the stipulations of counsel, the exhibits, the testimony of the witnesses, and the briefs of counsel, hereby makes and enters the following Findings of Fact and Conclusions of Law, pursuant to Rule 52(a), Fed.Rules Civ.Proc., 28 U.S.C.A.:

This is an action by the Trustees in Bankruptcy of Twin City Construction Company, Inc., against Pioneer Bank & Trust Company of Shreveport, Louisiana, seeking to recover the total sum of $69,145 alleged to have been received by defendant and claimed to be voidable transfers under Sections 60, sub. b and 67, sub. d of the Bankruptcy Act, 11 U.S.C.A. §§ 96, sub. b, 107, sub. b. The items sought to be recovered logically and conveniently should be placed in three separate categories as to which separate Findings of Fact and Conclusions of Law will be entered. They are as follows: (1) A claim for $50,125; (2) another for $9,000; and, (3) still another for $10,020. Preliminary to summation of the detailed facts and a statement of our particular conclusions of law, the following general background statement is made for a clearer understanding of the nature of this proceeding.

General Statement

An involuntary petition in bankruptcy was filed against W. A. Gray, d/b/a W. A. Gray Construction Company, on March 12, 1956, in proceeding No. 7729 on the Bankruptcy Docket of this Court. Thereafter, on March 21, 1956, he was adjudicated a bankrupt upon his voluntary petition. He died on May 7, 1956. An involuntary petition was also filed against Twin City Construction Company by the Home Indemnity Company on the 13th day of April, 1956, in proceeding No. 7751 on the Bankruptcy Docket of this Court, and on April 21, 1956, Twin City Construction Company voluntarily was adjudicated a bankrupt. Gray was the sole stockholder of Twin City Construction Company and to a large extent, during the times in question, commingled the affairs of that corporation with his individual business.

William Alton Gray for many years had engaged in the construction business under the name of W. A. Gray Construction Company. Outwardly, he appeared to be quite successful. Whatever financial difficulties he had, he was able successfully to cover up and surmount until January, 1956, when he concluded he could not continue in business.

When Pioneer Bank & Trust Company was organized in 1945 and opened for business, Gray became one of its depositors and customers. (R. 274, 276.) In the regular course of business, the Bank made many loans to Gray to finance his construction business, permitting him to start and carry forward individual construction contracts (see Exhibit D–15, listing Bank loans to Gray back to 1950). Throughout its course of dealings with Gray, and until January of 1956, the Bank had never sustained any loss on any loan made to him individually or to his business, W. A. Gray Construction Company (R–277). The account was handled by the Bank's President, Rupert Campbell, who approved loans (R–235), clearing such matters with the Discount Committee when necessary. It is apparent that those who did business with Gray had utmost confidence in his ability to meet his financial obligations. This included Home Indemnity Company, whose representative testified that he was willing to and did authorize the writing of the bond here involved, if Gray would give his personal indemnity (R–100). The Bank, in discussing various loan transactions with him, repeatedly asked for financial statements, which were not furnished, but his record of payment through the years was good and this request was not pressed. The Bank considered that the general securities it held were adequate to protect its loans.

The bonding company's representative, Mr. Scott, was much impressed with Mr. Gray's physical plant in June of 1955. The personal financial statement, introduced as Exhibit P–2, furnished to the bonding company at that time, was entirely satisfactory on its face. It showed a net worth of $293,952.45, but this did not accurately reflect the true situation.

Gray's affairs thus appeared outwardly to be not only solvent, but prosperous, to those with whom he dealt. His true financial status, however, as described by his office Manager, Preston Petty, presents an entirely different hindsight picture. Mr. Petty testified that if Mr. Gray had been forced to liquidate at any time after 1951, he would have been insolvent. Petty also testified as to the procedure followed by Gray so as to keep the Bank from learning of his true financial status (R–174, 175, 176). He also described how Gray would borrow and pay back and borrow again (R–176), always saying that they had worked out of a bad capital situation once and could do it again, e. g., "It may take four or five years, but we will pay out again." (R–147.) Petty also testified that Gray had no intention of ever "beating" anyone out of anything, but had to have capital and bonds and would do what it took to get a bond (R–147). Just prior to the collapse of his operations in January of 1956, Gray had as many as ten large government construction contracts going on in the State of Arkansas (R–191). He had money com-ing in on these government contracts and, undoubtedly, hoped to utilize the profits to recoup his negative capital situation.

As stated, the true capital condition known to Petty and Gray obviously was not communicated to the Bank (R–174–176). Gray had established a line of credit at the Bank, had posted collateral mortgages and pledges to secure loans to be made to him, and, in addition, when loans were made on individual contracts, a pledge was taken by the Bank covering the proceeds of the individual contract on which the loan was made (see Exhibit D–9, Pledge Agreement on $19,000 loan and, Exhibit D–10, Pledge Agreement on $10,000 loan). The Bank held as general collateral security a $40,000 mortgage on Gray's home, a $20,000 mortgage on his office building, a $20,000 mortgage on his equipment, a pledge of the stock of W. A. Gray, Inc., owner of the property known as Blair Apartments (R–209).

This shows the apparently substantial character of Gray's business and account with the Bank and justified the course of dealing and confidence the Bank's President had in him (R–210). His line of credit was such that the Bank, in the normal course of business, frequently honored payroll and materials checks, and other withdrawals, even though overdrafts often occurred (see Testimony of Mr. Friedman, R–251, 252).

1. The $50,000 Loan to W. A. Gray
And Its Repayment
Findings of Fact

1.

Twin City Construction Company, Inc., was organized in 1951. William A. Gray was the sole stockholder. This corporation had been dormant and conducted no business as such for several years (R–219).

2.

On May 28, 1955, Gray approached the Bank, through Mr. Campbell, and requested a loan of $50,000, stating that he had decided to reactivate Twin City Construction Company and that he thereafter was going to conduct his construction operations through Twin City Construction Company, Inc. In support of this request, Gray stated that his health had been poor and that he desired to do business on construction contracts in the corporate form to insure continuity and to avoid personal liability (R–220). He also stated that he expected to obtain additional capital from another party who had expressed a desire to enter the construction business with him (R–220). The evidence established that similar statements were made by Gray to representatives of the Home Indemnity Company when Gray made application for a bond on a construction contract at Blytheville, Arkansas, which was eventually awarded by the United States Government to Twin City Construction Company (see testimony of Mr. Scott, R–100).

3.

Pioneer Bank & Trust Company, at Gray's request, and relying upon his representations and upon its long continued course of satisfactory banking relations with him, made a loan of $50,000 as requested on May 28, 1955. The Bank took Gray's personal note for that amount, payable in fifteen days, to its own order (Exhibit P–3). The entire $50,000, at Gray's direction, was deposited simultaneously by the Bank in the checking account of Twin City Construction Company, Inc., maintained at Pioneer Bank (Exhibit P–4). Deposit slip dated May 28, 1955, in the amount of $50,150 was stipulated at the trial to include this $50,000. When this was done, the Bank held collateral mortgages on Gray's office and yard property, a $40,000 mortgage on his home and a pledge of all of the capital stock of the Blair Apartments.

4.

Pioneer Bank & Trust Company, through the $50,000 loan, in fact augmented the funds of Twin City Construction Company *pro tanto*. At no time was this sum, or any part of it, withdrawn from the bank account prior to its repayment to the Bank on June 8th or 9th, 1955, as hereinafter related. The sum of $50,125 which the Trustees seek to recover in this action is in fact the identical $50,000 constituting the proceeds of the loan referred to. But for the loan of $50,000.00 made by the Bank as above related, there would have been no asset or credit item in that amount reflected in the bank account of Twin City Construction Company, Inc.

5.

On the 8th day of June, 1955, Gray reported to the Bank that the purpose for which the loan had been made could not be carried out; and the transaction was closed by repayment of $50,125 to the Bank by check signed by Gray as President of Twin City Construction Company payable to the Bank (Exhibit P–6), covering the principal and accrued interest. The check was dated June 12, 1955, but actually was cleared on June 9, 1955. The issuance of the check by Gray in payment of the loans was in practical effect a reversal of the bookkeeping entry under which the $50,000 had been credited to the account of Twin City Construction Company, the entire transaction consuming only twelve days. Thus it is found as a fact that, within a period of only twelve days, the loan was made, the funds were credited to Twin City, the Bank was told the purpose was impractical and the exact money loaned was repaid to the Bank which had furnished it prior to its withdrawal. There can be no question as to Gray's authority to represent Twin City Construction Company, through proper board resolutions, in all of its transactions with the Bank (see Exhibits D–2, D–3, D–4), which in fact acted in good faith.

6.

Gray apparently issued stock to himself in Twin City Construction Company for $50,000, but the Bank was unaware of this at the time of the transaction. When it suited his purposes, Gray showed the stock to have been issued to himself. The Court finds as a fact that the Pioneer Bank & Trust Company had no knowledge of the issuance of the stock until a considerably later date, and knowledge thereof is not chargeable to the Bank during the period in question. We further find as a fact that the Bank had no knowledge of any intention that Gray may have had to issue $50,000 in stock to himself in return for the proceeds of the loan.

7.

Prior to June 15, 1955, Gray had made application, on behalf of Twin City Construction Company, to Home Indemnity Company for a Contractor's Performance Bond. On June 15, 1955, which was about a week after the $50,000 loan had been repaid to the Bank, Home Indemnity Company sent its representative, Mr. Scott, to Shreveport for the purpose of investigating the application. Mr. Scott called at the Pioneer Bank with a Mr. Parker, one of Home's local agents. From Scott's own testimony it is clear and undisputed that he asked the Bank for verification of the $50,000 balance, as shown in Twin City's financial statement furnished by Gray, as of May 31, 1955, and that the balance of $50,000 as of that date was thus verified, by an officer of the Bank who had not handled, and was not familiar with, the details of Gray's or Twin City's accounts. These representatives of the bonding company did not attempt to verify, or even inquire about, whether the $50,000 was on June 15, 1955, still on deposit in the account of Twin City Construction Company. This constituted gross carelessness on their part for if inquiry had been made as to the balance on June 15, 1955, the fact that the credit had been withdrawn and paid to the Bank would have been discovered, and undoubtedly the bond would not have been written. The Court finds that Mr. Lindsey was the representative of the Bank who on June 15, 1955, verified the statement as of May 31, 1955, as requested by Scott, and that neither Mr. Lindsey nor any other representative or officer of the Bank was in any way a party to any misrepresentation of any character to the representatives of the bonding company. The bond was not written until the 21st day of June, 1955, after Home Indemnity Company had conducted its own investigation and after it had satisfied itself with the personal guaranty of Gray. Gray also had given Home Indemnity Company the same reasons for converting his activities over to corporate form as he had given to Mr. Campbell, President of the Bank. The Bank was as much deceived by Gray's representations in this respect as was the bonding company.

8.

Pioneer Bank & Trust Company, by letter dated June 9, 1955 (Exhibit P–24), listed all of Gray's personal loans in a letter to Newark Insurance Company, another bonding company reinsuring a portion of the bond, which letter was dispatched late in the afternoon of June 9, 1955, and which was based on information compiled by the Loan and Discount Department of the Bank. The Court finds as a fact that the letter was issued in good faith and reflected the then existing facts under which the $50,000 loan had been previously repaid, and for this reason was not included in the list of outstanding loans chargeable against Gray. Gray undoubtedly used the credit balance of $50,000 on May 31, 1955, in setting forth assets of Twin City in making application for the bond written by Home Indemnity Company and he further used a financial statement and audit report showing that on May 31, 1955, there was a $50,000 bank balance to the credit of Twin City. The Bank was not a conscious party to any of these misrepresentations by Gray, but did furnish routine verification of balances as of May 31, 1955, the only date as of which verification was requested. Gray did not make disclosure to the Bank of any intention he may have had to use the bank balance of Twin City as a credit item to obtain a bond and the Bank was equally deceived by his fraudulent representations as to the intended purpose of the loan in that respect.

9.

The evidence does not support the factual contention made by plaintiffs that a representative of the Bank stated to the representative of the bonding company that there was no note of Gray supporting the $50,000.00 deposit or that the deposit of May 28, 1955, represented personal savings of Mr. Gray and not a loan. In this respect the Court believes the testimony of the Bank's witness denying that any such representation was made.[1]

10.

During the period when Twin City was activated by the action of Gray, that is, from May 28, 1955, until it was adjudicated a bankrupt on April 21, 1956, it had only one contract, the Blytheville, Arkansas, government contract. Home Indemnity Company, as its surety, eventually paid bills of Twin City in the approximate amount of $52,130.42 to complete the contract. The record does not establish that Twin City was insolvent as of the date of the repayment of the $50,000 loan to the Bank June 8, 1955, or as of June 22, 1955, when the bond of Home Indemnity Company was written.

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[1] Counsel for the trustees in their second reply brief argue: "The Bank, with full knowledge of Gray's shenanigans, informed Mr. Scott, of the bonding company, *before* the bond was written, that the $50,000 deposited in the account of Twin City was not the proceeds of any loan to Gray, knowing full well that it was, being a party to Gray's depositing the proceeds of the loan made by him to the account of Twin City". (Second Reply Brief, p. 2.) The Court does not accept this conclusion of fact, finding, on the contrary, that the preponderance of the credible testimony is to the effect that the Bank had no such knowledge of Gray's plans and no such misrepresentations were, in fact, made by the Bank.

Conclusions of Law

1.

Section 67, sub. d(6) of the Bankruptcy Act, with exceptions therein noted, annuls, in favor of the Trustees in Bankruptcy, those transfers which are fraudulent as defined in the Act. The applicable statutory provisions are:

> 67, sub. d(6) "A transfer made or an obligation incurred by a debtor adjudged a bankrupt under this title, which is fraudulent under this subdivision against creditors of such debtor having claims provable under this title, shall be null and void against the trustee, except as to a bona fide purchaser, lienor, or obligee for a present fair equivalent value: Provided, however, That the court may, on due notice, order such transfer or obligation to be preserved for the benefit of the estate and, in such event, the trustee shall succeed to and may enforce the rights of such transferee or obligee: And provided further, That such purchaser, lienor, or obligee, who without actual fraudulent intent has given a consideration less than fair, as defined in this subdivision, for such transfer, lien, or obligations, may retain the property, lien, or obligations as security for repayment."
>
> 67, sub. d(1)(e) "Consideration given for the property or obligation of a debtor is 'fair' (1) when, in good faith, in exchange and as a fair equivalent therefor, property is transferred or an antecedent debt is satisfied, or (2) when such property or obligation is received in good faith to secure a present advance or antecedent debt in an amount not disproportionately small as compared with the value of the property or obligation obtained."

2.

As is pointed out in Collier's Bankruptcy Manual, (Oglebay, Kelliher and Newkirk) (1948), p. 845, in discussing Section 67, sub. d:

> "Whether a fair consideration has been given for a transfer *must depend on all of the circumstances of the case.* Fairness in every case is largely a question of fact, *as to which considerable latitude must be allowed to the trier of the facts.*" (Emphasis supplied.)

3.

The Bankruptcy Act defines the terms "debt" and "creditor" in Section 67, sub. d(1) as follows:

> "(d) For the purposes of, *and exclusively applicable to, this subdivision*: . . . (b) 'debt' is any legal liability, whether matured or unmatured, liquidated or unliquidated, absolute, fixed, or

contingent; . . . (c) 'creditor' is a person in whose favor a debt exists." (Emphasis supplied.)

4.

Pertinent and applicable articles of the LSA–Civil Code include the following:

Article 1896: Cause and want of cause defined.—"By the cause of the contract, in this section, is meant the consideration or motive for making it; and a contract is said to be without a cause whenever the party was in error, supposing that which was his inducement for contracting to exist, when in fact it had never existed, or had ceased to exist before the contract was made."

Article 2292: "Certain obligations are contracted without any agreement, either on the part of the person bound, or of him in whose favor the obligation takes place.

"Some are imposed by the sole authority of the laws, others from an act done by the party obliged, or in his favor.

"The first are such engagements as result from tutorship, curatorship, neighborhood, common property, the acquisition of an inheritance, and other cases of a like nature.

"The obligations, which arise from a fact, personal to him who is bound, or relative to him, result either from quasi contracts, or from offenses and quasi-offences."

Article 2293: "Quasi contracts are the lawful and purely voluntary act of a man, from which there results any obligation whatever to a third person, and sometimes a reciprocal obligation between the parties."

Article 2294: "All acts, from which there results an obligation without any agreement, in the manner expressed in the preceding article, form quasi contracts. But there are two principal kinds which give rise to them, to wit: The transaction of another's business, and the payment of a thing not due."

Article 2300: "All persons, such even as are incapable of consent, may, by the quasi contract, resulting from the act of a third person, become either the object or the subject of an obligation; because the use of reason, although necessary on the part of the person whose act forms the quasi contract, is not requisite in those by whom, or in whose favor, the obligations resulting from the act, are contracted."

Article 2301: "He who receives what is not due to him, whether he receives it through error or knowingly, obliges himself to restore it to him from whom he has unduly received it."

Article 2315: "Every act whatever of man that causes damage to another, obliges him by whose fault it happened to repair it; . . ."

5.

Under the provisions of the Bankruptcy Act relied upon by plaintiffs a transfer within one year prior to the filing of a petition in bankruptcy is not fraudulent unless it is made or incurred "without fair consideration".[2] In light of the statutory definition of fair consideration as that term is used in the Bankruptcy Act above quoted, the Court finds as a conclusion of law that the repayment to the Pioneer Bank & Trust Company of the $50,000 loan under the facts and circumstances of this case cannot be said to be "without fair consideration" as that term is used in Section 67, sub. d(2) and for the basic reason, in addition to the reasons further stated, an essential element of a voidable transfer is lacking under the Act. The Court also finds that the repayment made to the Bank of the identical bookkeeping credit reflecting the proceeds of the loan never withdrawn was as a matter of law supported by a fair equivalent in value under Section 67, sub. d(6) in that the transaction must, under the provisions of law quoted, be viewed in its entirety and in its net effect. In applying these provisions of the Bankruptcy Act this Court must consider the fact that the Bank was repaid the identical money it had furnished to Gray in the Twin City account. If Gray had not repaid the Bank but had revealed the facts to it, there would have been a legal obligation on the part of Twin City to make the reimbursement. In other words, the circumstances under which the loan was made were sufficient under the law of Louisiana to give rise to an antecedent indebtedness from Twin City Construction Company to the Bank. Such liability on the part of Twin City properly may be predicated either upon the principle of quasi contract (unjust retention of a benefit) or delictual responsibility. See the Civil Code Articles above cited.

Though the facts establish that the loan was initially made on the credit of Gray, the proceeds inured only to the benefit of Twin City and the loan was made for a specific and definite purpose, to-wit: to enable Gray thereafter to carry out his construction business as Twin City Construction Company instead of as W. A. Gray Construction Company. The purpose for which the loan was made having failed, according to the representations made by Gray to the Bank, and accepted by the Bank in good faith, established, under the quoted Articles of the Louisiana Civil Code, a legal right in the Bank to demand reimbursement from Twin City of the proceeds of the loan. If the Bank had the legal right to compel Twin City to make reimbursement when Gray stated the purpose of the loan had failed, the action of Gray in causing the loan to be paid was not a transfer "without fair consideration" within the meaning of Section 67, sub. d(2) of the Bankruptcy Act. Moreover, the Court finds that the Bank was deceived by the active misrepresentations of fact made by Gray and Twin City, therefore, would be liable delictually to make reimbursement to the Bank. The liability so resulting constitutes a "debt" as that term is broadly and specially defined in the Bankruptcy Act and entitles the Bank to the protection afforded to a bona fide "obligee" under the statute. The numerous authorities sustaining a corporation's liability for fraud are collected in 19 Corpus Juris Secundum, Section 1278. The Bankruptcy Act recognizes that satisfaction of an "antecedent debt" is one meaning of the term giving a "fair" consideration for the property. The circumstances of this case are unusual and the Court, viewing the matter in its entirety, considers that this is, in fact and in law, a situation in which the Court is called upon to exercise the traditional equity powers of a Court of Bankruptcy. The Court recognizes that normally a transfer made to benefit a third party is not made for a "fair" consideration.

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[2] "Every transfer made and every obligation incurred by a debtor within one year prior to the filing of a petition initiating a proceeding under this title by or against him is fraudulent . . . (b) as to then existing creditors and as to the other persons who become creditors during the continuance of a business or transaction, *if made or incurred without fair consideration* by a debtor who is engaged or is about to engage in such business or transaction, for which the property remaining in his hands is an unreasonably small capital, without regard to this actual intent; . . .". § 67, sub. d (2) (b), 11 U.S.C.A. § 107, sub. d (2) (b). (Italics supplied.)

6.

This is not the normal case in which diversion of corporate assets for the payment of the indebtedness of another calls for application of the rule that such a transfer is not supported by a "fair consideration". Authorities cited by plaintiffs, including Davis v. Hudson Trust Company, 3 Cir., 1928, 28 F.2d 740, and related cases are thus not in point. In none of the cases cited by plaintiffs was it established that the item sought to be recovered by the trustee in bankruptcy consisted of funds originally supplied by the defendant transferee from whom recovery was sought. The distinguishing factor making inapplicable the authorities relied upon by plaintiffs is that equitably and legally Twin City here was obligated to make reimbursement to the Bank. The satisfaction of that obligation was satisfaction of an antecedent indebtedness within the meaning of the applicable provisions of the Bankruptcy Act, both in the definition of voidable transfers and in the protections afforded a bona fide obligee by the applicable provisions of the Chandler Act.

7.

The provisions of Section 67, sub. d (2)(d) invalidating transfers made with "actual intent" to "hinder, delay, or defraud either existing or future creditors" are, in the view of the Court, not applicable to the repayment of this $50,000 to the Bank under the circumstances that were present. There is no clear and convincing proof that in making the repayment Gray made it with actual intent to defraud the future creditors of Twin City Construction Company. Gray's fraud rather consisted in obtaining the bond by false representations. Once he had laid the basis for obtaining the bond, there is reason to believe that he did not consider that the repayment of the $50,000 to the Bank would affect his ability to carry out his contract at Blytheville, Arkansas, at a profit. He was utilizing the Gray organization and its central overhead and, to some extent, its credit position and it is more logical to conclude that he did not have the conscious and deliberate intent to defraud required by Section 67, sub. d(2)(d). The transfer was in payment of Gray's note to the Bank, but, as pointed out above, the transfer also satisfied an indebtedness of Twin City to the Bank. The circumstances all combine to support the inference that Gray was motivated by a desire to continue his business and to rehabilitate himself financially. The Court accepts Petty's testimony that Gray actually intended to pay his creditors, because he had worked out of bad situations before. The Court finds, therefore, that the repayment was not with actual intent to defraud. However, even if it be considered as part of an entire fraudulent transaction, the Court is of the opinion that the transfer is protected by Section 67, sub. d(6) which protects an obligee who, without actual fraudulent intent, accepts a transfer based upon an antecedent debt. The Bank was in good faith in accepting the payment. The Court concludes that the Bank, under the circumstances, is a "bona fide" obligee within the proviso and protection of Section 67, sub. d(6). Collier, Bankruptcy Manual, p. 858, states:

> "This proviso comes into play only after it has been determined that there has been a fraudulent conveyance and that the transferee is not a *bona fide* purchaser, lienor or obligee for a *present* fair equivalent value. Notwithstanding the absence of 'good faith' or 'a present' fair equivalent value, the transferee obtains protection to the extent of the consideration given by him if he can demonstrate his innocence of any intent to participate in the fraud perpetrated on the transferor's creditors. The new proviso seems to protect a transferee who without actual fraudulent intent has extinguished or accepted security for a debt owing by the bankrupt. If the antecedent debt amounts to a fair equivalent of the property transferred therefor, the transfer will presumably be upheld in full, although the transferee is technically not a 'bona-fide purchaser, lienor, or obligee for a *present* fair equivalent value'." (Emphasis supplied.)

As a *bona fide* obligee of Twin City, the Bank, the Court concludes, is entitled to retain the payment of funds represented by a reversal of the bookkeeping transfer when the check was issued to the Bank.

In the last analysis under the facts at issue, all that the Bank did was to receive reimbursement of a loan which it had made in good faith based on representations which did not reflect the true purpose in making the loan. The money was repaid within twelve days and never left the bank account. The Court does not believe the Chandler Act literally requires the Bank to repay the trustees under these circumstances. The harsh result contended for by the trustees is not within the intendment or purpose of the Statute. Recovery for the $50,125.00 item will, accordingly, be denied.

8.

The Court does not consider the cases cited by petitioners in their brief support any right of recovery by the trustees under the circumstances here found. There does not seem to be direct judicial authority in which a recovery under the exact circumstances here involved was sought by a trustee in bankruptcy under Section 67, sub. d. Implications from cases to which analogy might be made would deny any right of recovery as applied to the facts before the Court and the Court deems this to be the correct conclusion applicable to the circumstances at bar. See Malone v. Gimpel, D.C. N.D.N.Y. 1956, 151 F.Supp. 549, affirmed by the 2 Cir., 1957, 244 F.2d 954; Newfield v. Stieglitz, D.C.1942, 47 F.Supp. 885, affirmed Newfield v. Oosterhuis, 2 Cir., 137 F.2d 437; Cf. In re Venie, D.C. 1948, 80 F.Supp. 250.

The Court understands that counsel for the trustees have abandoned their contentions seeking recovery on the ground that the $50,000 repayment was *ultra vires*. Accordingly, the legal issues involved as to that aspect of the case will not be commented upon other than to say that they have been carefully considered by the Court and are found not to detract from the conclusions reached by the Court under the applicable bankruptcy statutes. The Court does not consider that the Uniform Fiduciaries Act, LSA–R.S. 9:3808, is here applicable in view of the full authority vested in Gray by the resolutions on file with the Bank and in further view of the fact that the repaid item of $50,000 was the same money which the Bank had placed in the account of Twin City at Gray's request when he made the loan.

II. The $9,000 Transfer To The William A. Gray Account

Findings of Fact

1.

On December 28, 1955, within four months of the filing of the involuntary bankuptcy petition against Twin City Construction Company, Gray instructed the Pioneer Bank to transfer the sum of $9,000 from the checking account of Twin City Construction Company, maintained with the Bank, to the bank account of William A. Gray. A loan in the amount of $10,000 had been made by the Bank the same day and deposited to the account of Twin City Construction Company. The transfer was made by debit memorandum as per instructions. In issuing such instructions, Gray acted as President of Twin City Construction and acted pursuant to his full authority as evidenced by corporate resolutions furnished to and on file with the Bank (Exhibits D–2 & D–3). The Bank in good faith relied upon the authority vested in Gray in making the transfer pursuant to his request.

2.

The $9,000 so transferred inured to the benefit of W. A. Gray Construction Company in that it was used to cover disbursements made and charged to the checking account of W. A. Gray Construction Company. At the time of the transfer there was an overdraft in the account of W. A. Gray in the amount of $4,398.69 which had occurred in the normal course of business of W. A. Gray Construction Company. The balance, in the main, cleared disbursements made by W. A. Gray Construction Company to third parties.

3.

Overdrafts were not unusual in the normal conduct of the business of W. A. Gray Construction Company and deposits to cover overdrafts were frequently and normally made in connection with the handling of the checking account of W. A. Gray. The record establishes that such overdrafts occurred almost daily and it was the normal practice to cover such overdrafts by deposits in the W. A. Gray Construction Company account.

4.

The Bank did not, in fact, receive the $9,000 deposited in the checking account of W. A. Gray Construction Company but such funds were credited to the checking account of W. A. Gray Construction Company and were utilized to balance the account, including the payment of overdrafts.

5.

The Court finds as a fact that there was a considerable degree of commingling of the affairs of W. A. Gray Construction Company and Twin City Construction Company. The same office was occupied, the same personnel and central overhead staff was employed, and Gray, in practice, was using the W. A. Gray Construction Company in connection with the Twin City Blytheville contract being carried out.

6.

In the handling of the account of W. A. Gray Construction Company, including the crediting of the $9,000 to that checking account, the Bank had no reasonable cause to believe that either Gray or Twin City Construction Company was insolvent on December 29, 1955, when the debit memorandum transfer was effected. The insolvency of Twin City Construction Company as of that date is not conclusively shown. In accepting the deposit of $9,000, in giving the credit, and by paying the items subsequently paid and covering the previously paid items included in the overdraft, the Bank acted in good faith and furnished a fair consideration in the form of such payments and bank clearances. In keeping with the practice in such matters the withdrawal of Gray was later entered as a receivable from Gray but it is clear that Gray was insolvent at the time. The Bank did not have reasonable cause to believe that Gray was insolvent on December 29, 1955.

Conclusions of Law

1.

The Trustees in Bankruptcy attacked the transfer of $9,000 above referred to under Section 67, sub. d(2) and also as voidable under State law by virtue of the provisions of § 70, sub. e(1), 11 U.S.C.A. § 110, sub. e(1).

2.

Without dispute, W. A. Gray had authority to make the transfer of the $9,000 pursuant to resolutions on file with the Bank and the Bank, as a matter of law, was entitled to rely upon that authority, including the provision in the corporate resolution of authority which provides as follows:

> "Be It Further Resolved, That W. A. Gray, President, be and he is hereby empowered and authorized to do any and all acts whatsoever on such terms and conditions and for such considerations, within his discretion, that this corporation could do if a natural person, this authority conferred being intended to authorize the said W. A. Gray as President to represent this corporation in all matters whatsoever and to confer on him the fullest possible powers in such representation."

3.

Under section 67, sub. d(2) of the Bankruptcy Act, if the Bank has furnished "a fair consideration" for the transfer of the $9,000 by debit memorandum, the transaction is excepted from the reach of Section 67, sub. d(2) and is not voidable in an action brought by the trustees. Interpreting and applying Section 67, sub. d(2) to the facts, the Court concludes that the crediting of the account of W. A. Gray Construction Company with the $9,000 and the clearance of items against that credit, including clearance of the $4,398.69 overdraft which had occurred in the normal and regular course of business, was the furnishing of a "fair consideration". Whether fair consideration is present in a particular case depends on all the facts and circumstances. See 4 Collier on Bankruptcy, Sec. 67.33, pp. 345–350. Because of the commingling of the affairs of

Twin City Construction Company with those of W. A. Gray Construction Company and because of Gray's status as sole stockholder with full corporate authority (D–3) upon which the Bank actually relied, the Bank could not, in its dealings with him, have disregarded that authority especially where it had positive knowledge that the funds being transferred were in fact being used to cover clearances against the bank account representing, in the main, items payable by W. A. Gray Construction Company in connection with its construction business. By accepting the deposit, by giving the credit, and by paying the items already overdrawn, in good faith, the Court concludes as a matter of law that the Bank was furnishing a fair consideration for the deposit so received.

4.

The Uniform Fiduciaries Act adopted in Louisiana as LSA–R.S. 9:3801 et seq. does not entitle the trustees to recover under Section 70, sub. e(1) of the Bankruptcy Act. The purpose of the Uniform Fiduciaries Act is to protect a depository bank which acts in good faith without positive knowledge that a breach of trust is being committed. The act even recognizes the right of a fiduciary to transfer the funds from a fiduciary account to his personal account, LSA–R.S. 9:3809. The Pioneer Bank & Trust Company was not required to make inquiry as to whether the fiduciary (W. A. Gray) was committing a breach of his obligation in transferring funds from the bank account of Twin City to that of W. A. Gray Construction Company. Especially is the Uniform Fiduciaries Act here applicable to protect the defendant Bank because the record establishes that it was making loans in good faith to both Gray and the corporation to finance construction contracts being carried out by Gray and Twin City and in practical effect Gray was Twin City.

5.

In the relationship between Bank and depositor, the Courts, in applying Section 60, sub. b of the Bankruptcy Act have looked with favor upon the position of the depositary bank and have protected the bank even when an insolvent depositor makes deposits in the course of business to cover an overdraft. Although the circumstances involved in this $9,000 transaction do not involve a voidable preference, the Court concludes that what occurred, under all of the facts and circumstances, cannot be viewed as a voidable transfer to the Bank within the meaning of Section 67, sub. d(2).

6.

Interpreting and applying 67, sub. d (2) (b), and (c) to the facts of this case, an important fact preventing recovery by the Trustees in Bankruptcy for this item is that this $9,000 was not transferred to the Pioneer Bank. The money was transferred to the checking account of W. A. Gray Construction Company and in fact inured to the benefit of W. A. Gray. The Bank was merely a depositary conduit through which the money passed. In this connection, the Court observes that in Civil Action No. 5445, on the Docket of this Court, the complainants, as Trustees of W. A. Gray Construction Company are seeking recovery of the same $4,398.69 overdraft on the theory that it was money belonging to Gray improperly paid to the Bank as a preference. Applying the law to the facts, we reach the conclusion that the $9,000 so transferred was transferred to W. A. Gray Construction Company and not to the Bank and we find no facts and circumstances to justify a recovery of any portion of the $9,000 item predicated upon any of the provisions of Section 67, sub. d(2) of the Bankruptcy Act.

The trustees have cited Articles 1970, 1971, 1980, 1984 and 1985 of the LSA–Civil Code of Louisiana and the decision of this Court in Mayo v. Petty, D.C. 1957, 153 F.Supp. 501, in favor of the Trustees in Bankruptcy, setting aside a deed as a voidable preference and a constructive fraud. The Court has considered these provisions of law and finds that they are not applicable to the facts here. Their application in Mayo v. Petty was to circumstances quite distinguishable from the facts before us, as will appear from that decision.

III. The $10,000 Pledge-Agreement Repaid Loan Of Twin City Construction Company

Findings of Fact

1.

On December 29, 1955, Twin City Construction Company borrowed $10,000 from the Pioneer Bank & Trust Company. Simultaneously with the loan, the Bank took a pledge agreement in keeping with its usual practice in making loans to finance construction contracts of W. A. Gray (Exhibit D–10). The written pledge agreement given by Twin City to the Bank, under date of December 29, 1955, specifically recites: "We pledge the balance due on this contract to secure a loan in the amount of $10,000.00 for a period of thirty (30) days." (See last paragraph of Exhibit D–10.) The contract referred to, covered by the pledge, was the government contract for the rehabilitation of buildings at the Blytheville, Arkansas, Air Force Base.

2.

The loan was made to Twin City Construction Company within the four months period prior to the filing of the involuntary bankruptcy petition against Twin City Construction Company. Twelve days after the loan was made, the proceeds thereof were made available to Twin City Construction Company, the loan was repaid in full on January 10, 1956, by debit memorandum against the account of Twin City Construction Company in the amount of $10,020 (Exhibit D–14).

3.

The Court finds as a fact that the payment of January 10, 1956, was made by Twin City in full recognition and confirmation of the validity of the pledge agreement of December 29, 1955, the payment having come directly from the proceeds of a check of the United States Government in the amount of $11,693.18 (Exhibit D–13), which was deposited to the account of Twin City Construction Company (see Exhibit D–12). The Court further finds as a fact that the $10,020 payment of the note was made on the same date and in connection with the deposit of the proceeds of the government contract as referred to and the Bank thereupon marked the note paid and returned it to Twin City Construction Company.

4.

The Court further finds as a fact that the debit memorandum of $10,020 was merely the means whereby Twin City Construction Company elected to carry out its obligation of recognizing and ratifying the pledge agreement under which the collected proceeds were required to be made available to the Bank in settlement of the loan that had been made only twelve days earlier.

5.

Notice of the letter pledge agreement above referred to was not given to the United States Government; but thereafter, within a period of twenty-one days from the date of the loan, to-wit, on January 10, 1956, twelve days after the loan, the proceeds of the government contract were paid to Twin City Construction Company and utilized by it to the extent of the $10,020 which retired the note.

Conclusions of Law

1.

The Trustees in Bankruptcy seek recovery of the $10,020 payment as a voidable preference under Section 60, sub. b of the Bankruptcy Act. The position of the Bank is: (1) that the letter pledge agreement of December 29, 1955 (Exhibit D–10), created a valid pledge so that the payment to the Bank, a secured creditor, was not preferential; (2) it is further contended by the Bank that even if the pledge did not create a valid pledge initially for lack of notice to the Government, the pledge was thereafter perfected by actual receipt of the money within twenty-one days from the date of the loan and act of pledge; (3) that noncompliance with the Federal Assignment of Claims Act does not affect the Bank's right. These contentions are all disputed by the trustees.

2.

Under the provisions of Section 60, sub. a(7) of the Bankruptcy Act, if it be conceded *arguendo* that the letter pledge agreement required additional action by the Bank to protect its security interest under the written pledge, it nevertheless clearly appears that the repayment of the money to the Bank (i.e., reducing the pledged fund to possession) had the legal effect of protecting and perfecting the lien of the pledgee and if this was accomplished within twenty-one days of the original loan, the transaction is protected by the Bankruptcy Act. Section 60, sub. a(7) provides:

> "(7) Any provisions of this subsection a to the contrary notwithstanding, if the applicable law requires a transfer of property other than real property for or on account of a new or contemporaneous consideration to be perfected by recording, delivery, or otherwise, in order that no lien described in paragraph (2) of this subsection could become superior to the rights of the transferee therein . . . the time of transfer shall be determined by the following rules:
>
> "1. Where (A) the applicable law specifies a stated period of time of not more than twenty-one days after the transfer within which recording, delivery, or some other act is required, and compliance therewith is had within such stated period of time; or where (B) *the applicable law specifies no such stated period of time* or where such stated period of time is more than twenty-one days, and compliance therewith is had within twenty-one days after the transfer, the transfer shall be deemed to be made or suffered at the time of the transfer. . . ." (Emphasis supplied.)

It is plain that under Section 1(30) (11 U.S.C.A. § 1, as amended) of the Bankruptcy Act the term "transfer" includes the fixing of a lien or the perfection of a security interest. That section of the statute reads:

> "(30) *'Transfer' shall include* the sale and every other and different mode, direct or indirect, or disposing of or of parting with property or with an interest therein or with the possession thereof or of *fixing a lien upon property or upon an interest therein,* absolutely or conditionally, voluntarily or involuntarily, by or without judicial proceedings, as a conveyance, sale, assignment, payment, *pledge,* mortgage, *lien,* encumbrance, gift, security, or otherwise; the retention of a security title to property delivered to a debtor shall be deemed a transfer suffered by such debtor;. . . ." (Emphasis supplied.)

Section 60, sub. a(7) of the Bankruptcy Act was amended in 1950 to clarify and change the rule of law announced by the Supreme Court in the Klauder case, Corn Exchange Nat. Bank & Trust Co., Philadelphia v. Klauder, 318 U.S. 434, 63 S.Ct. 679, 87 L.Ed. 884. (See Collier, Manual of Bankruptcy Law, 1951 Supplement Section 60.121, discussing the Klauder case and the effect of the 1950 amendment.) Prior to the 1950 amendment if the Bank had made a loan to Twin City Construction Company within the four months period and taken a pledge agreement covering the contract proceeds, but it failed to notify the debtor of the credit (assuming Louisiana requires such notification), the Bankruptcy Act recognized the pledgee's lien as perfected only when the security interest was perfected by the required notice (or by the delivery to the pledgee of the thing pledged or by the payment of the money). The 1950 amendment had for its purpose the protection of those transactions which were inchoate, but were perfected within twenty-one days. It is the Court's conclusion that Louisiana law specifies no period of time in which the pledge of proceeds of a contract must be perfected by notice to the obligor. Consequently, under the literal provisions of Section 60, sub. a(7), the Bank, in making the loan to Twin City, in harmony with the Bankruptcy Act, could have perfected its lien under State law by notice to the debtor or by obtaining the proceeds within twenty-one days, the latter being not only a perfection, but a satisfaction of the lien. Cf. LSA–Civil Code Articles 3156, 3157, 3152 and 3153. It is our conclusion, in applying Section 60, sub. a(7) to the facts here found, that this is not a voidable preference, as a matter of law, because in receiving the payment the Bank was only doing what the Bankruptcy Act expressly permits and what State law sanctions. A more complete discussion of this subject and the relationship of this problem to the Klauder case and its background is found in Collier's Bankruptcy Manual (1951 Supplement), paragraphs 60.121 et seq. We conclude that the facts call for the application of Section 60, sub. a(7) and that the protection of that provision is directly applicable and available to defendant here. Even if it be conceded, as counsel for the trustees have argued, that the Bank's pledge was not complete for lack of notice to the obligor, the Government, its payment of the proceeds and Twin City's application thereof to the debt it had endeavored to secure, for a contemporaneous consideration—the loan—served to perfect the lien under a fair and reasonable interpretation of the Bankruptcy Act, in the light of the 1950 amendment.

3.

While the Court does not consider it necessary to base its conclusion denying recovery of the $10,000 item upon the validity of the original pledge, the Court nevertheless concludes on the basis of LSA–R.S. 9:4321-4323 that the letter pledge agreement executed in favor of defendant would of itself be sufficient to constitute a valid pledge without the necessity of notification to the debtor. That statute does not appear affirmatively to require the formality of notice to the debtor to make the pledge valid as to third persons. Only the obligor, whose obligation is intended to be pledged, is intended to be protected by the requirement of notice, "to bind the obligor to pay the amount due to the pledgee" (LSA–R.S. 9:4323). When this provision is considered in the light of the repealing clause, in Section 2 of Act 95 of 1938, it appears to the Court that the Louisiana Statute relied upon by defendant is sufficient to entitle the Bank to the status of a secured creditor under Louisiana law. It follows that the payment to the Bank was not preferential and voidable.

4.

In opposition to these conclusions of law it has been argued that there can be no valid assignment or pledge of a claim against the United States Government under a government contract without compliance with the provisions of Assignment of Claims Act, 31 U.S.C.A. § 203, and that any such attempted pledge is void. National Bank of Commerce of Seattle v. Downie, 1910, 218 U.S. 345, 31 S.Ct. 89, 54 L.Ed. 1065. The Court finds that the Downie case is not applicable and that this aspect of the argument of the trustees is disposed of adversely to their contentions by the case of M. M. Landy, Inc., v. Nicholas, 5 Cir., 221 F.2d 923, 927, 53 A.L.R.2d 1385, where the Court held:

> "We conclude, then, that failure to comply with the Federal Assignment of Claims statute is immaterial in the decision of this case. By stipulation, Landy's security interest is not protected by the methods provided by this statute. Nevertheless, we recognize that there may be alternative ways of perfecting a security interest in a claim against the Government, under State law, which are valid as against a trustee or receiver in bankruptcy."

In our view, the pledge of the proceeds of a government contract is not voidable, although the provisions of the Federal Statute have not been complied with procedurally, if it appears that the proceeds of the claim pledged and assigned actually have been reduced to possession and no interest on the part of the Government is involved. In other words, that Statute is purely for protection of the Government. See Martin v. National Surety Company, 1937, 300 U.S. 588, 57 S.Ct. 531, 81 L.Ed. 822, holding, in effect, that assignments will be recognized as valid, even though not in conformity with the Federal Statute, if the proceeds have been collected and the matter is thus beyond the original purpose of affording protection to the Government. The conclusions which we reach, in our view, are amply supported by an extensive annotation found in 12 A.L.R.2d 468. To sum up, we conclude that the Assignment of Claims Statute is only for the protection of the Government and that as between the parties herein no government interest is involved. An assignment which is valid under local law will be recognized against the claim of a trustee in bankruptcy where a valid pledge exists under local law.

5.

Even should this Court conclude that the Bank is not a secured creditor, under Federal law applicable to set-offs it would follow that the Bank would be protected on the $10,020 payment for it held the note of Twin City Construction Company and would have been entitled to offset the deposit against the note. See the following cases: New York County Nat. Bank v. Massey, 1904, 192 U.S. 138, 24 S.Ct. 199, 48 L.Ed. 380; Studley v. Boylston Nat. Bank, 229 U.S. 523, 33 S.Ct. 806, 57 L.Ed. 1313; American Bank & Trust Co. v. Morris, 5 Cir., 1927, 16 F.2d 845; Hill v. Jersey Shore State Bank, U.S.D.C.Pa.1949, 87 F.Supp. 129; Kane v. First National Bank of El Paso, Texas, 5 Cir., 1932, 56 F.2d 534, 536, 85 A.L.R. 362, certiorari denied, Kane v. Pottorff, 287 U.S. 603, 53 S.Ct. 8, 77 L.Ed. 524; Citizens' National Bank of Gastonia, N. C. v. Lineberger, 4 Cir., 1930, 45 F.2d 522; Fourth National Bank of Wichita, Kan. v. Smith, 8 Cir., 1916, 240 F. 19; Drugan v. Crabtree, 4 Cir., 1924, 299 F. 115. This Court recently applied this principle in the case of Harper v. First National Bank of Mansfield, D.C. — F.Supp. —. On the same subject matter, 3 Collier on Bankruptcy (15th Edition) pp. 760 et seq., we find the following:

> "Obviously, where the bank has not knowledge or imputation of knowledge, or 'reasonable cause to believe' that the depositor is insolvent, such routine deposits are clearly available as setoffs. *But even though the depositor was insolvent and knowledge of this fact could be charged against the bank at the time when the deposit was made, the bank is still entitled to apply the deposit on its claim, so long as it was accepted in good faith, in the ordinary course of business.* It is only where affairs have reached such a point that the bank accepts the deposit for the purpose of payment or of giving itself a subsequent advantage over other creditors through its right of set-off, or for some other special purpose, that the deposit and the subsequent application of it amounts to a recoverable preference." (Emphasis supplied.)

6.

Summarizing our conclusions of law as to this claim the Court finds that the requisites of a voidable preference, under Section 60, sub. b, are not present. It is the conclusion of the Court that the Bank had a valid security interest, that it perfected its lien by receiving payment within twenty-one days, and that the Federal Assignment of Claims Statute is no obstacle to recognition of the position of the Bank as a secured creditor. For these reasons, the Court concludes that there is no merit in the claim of the trustees for the recovery of this item.

For all of the foregoing reasons, plaintiffs are not entitled to recover from defendant on any of their claims.

A proper decree should be presented on notice.

Banking Commissioner's Authority to Pass on New Branches Upheld

A Texas savings and loan association brought suit against the state's banking commissioner for a declaratory judgment that the association could open branches without the commissioner's prior approval and for an injunction restraining the commissioner from taking any action to prevent the association from opening and operating six branch offices. The trial court determined that the association had opened one branch and made substantial commitments to open five others before the commissioner had adopted rules and regulations requiring his approval of proposed branch offices.

The appellate court ruled in favor of the commissioner. Specifically, it denied the declaratory judgment requested by the association, ruled that the commissioner's rules requiring his approval to open branches was valid and that these specific rules did not apply to the association's six branches because action to establish them was taken before the rules were adopted. Despite the inapplicability of the rules to this specific situation however, the court further ruled that the lower court erred in enjoining the commissioner from taking steps to interfere with the opening of the association's six branches because he had the power to approve or disapprove branches from his general statutory authorization to supervise and control such banking associations. *Falkner v. Southwestern Savings and*

NOTE—For similar decisions see B. L. J. Digest (Fifth Edition) § 119.

Loan Association of Houston, Court of Civil Appeals of Texas, 320 S.W.2d 164. The opinion of the court is as follows:

GRAY, J.—Southwestern Savings and Loan Association of Houston, Texas, brought this suit against J. M. Falkner, Banking Commissioner of the State of Texas, and prayed for a declaratory judgment decreeing that it may open branch offices without first obtaining the approval of the Commissioner, and for an injunction restraining the Commissioner from taking any action to prevent it from opening and operating branch offices.

By his answer the Commissioner affirmatively claimed statutory authority to require his approval prior to the opening of branch offices, and further alleged the promulgation of rules and regulations requiring the prior approval of the Commissioner for the opening of branch offices of State building and loan associations.

At a nonjury trial judgment was rendered denying the declaratory judgment prayed for in part but finding that "there was no prohibition in the statutory provisions, legal restrictions and other laws of the State of Texas against the plaintiff opening a branch office or branch offices . . . without obtaining the prior approval of the Banking Commissioner of the State of Texas;" and holding that "upon the abovementioned rules and regulations being adopted the Plaintiff became bound to obtain the prior approval of the State Banking Commissioner before opening any branch office other than the six branch offices mentioned specifically in this judgment" and enjoining the Commissioner from interfering with the opening of six branch offices by Southwestern.

Southwestern has appealed from that part of the trial court's judgment denying a declaratory judgment and the Commissioner has appealed from that part of the judgment granting injunctive relief and also complains of findings made by the trial court.

The facts show that Southwestern is a building and loan association incorporated and existing under the laws of Texas with its office and principal place of business located at 3401 South Main Street, Houston, Texas. It desired to open five branch offices in the City of Houston and one in the adjoining suburb of Bellaire and by letter dated December 30, 1953, and presented to the Commissioner on January 7, 1954, it notified the Commissioner of its intention to open such branch offices and gave their proposed locations.

At the time of the trial one of such offices had been opened and commitments for opening the others had been made.

This suit was filed December 10, 1957 and on January 29, 1958 rules and regulations were promulgated and adopted requiring the approval of the Commissioner prior to the opening of branch offices of building and loan associations. The rules provided that an application shall be filed for permission to open additional public offices which shall state:

> ". . . the need therefor; the functions to be performed; the personnel and office facilities to be provided; the estimated annual volume of business, income and expenses of such additional public office; and shall be accompanied by a proposed annual budget of the applying association."

The rule then provides that the application shall be set for hearing, notice given as is provided for new charter applications and further provides that the application shall not be granted unless the Commissioner shall affirmatively find stated requirements.

The trial court held that the above rules were valid and binding on Southwestern after their effective date but that because Southwestern had opened or had made substantial commitments for opening the proposed offices prior to January 29, 1958, said rules had no application to such proposed offices. The judgment was entered July 1, 1958.

Southwestern complains that the trial court erred in holding that the Commissioner had authority to promulgate rules requiring building and loan associations to obtain prior approval of the Commissioner before opening public offices other than its home office.

Art. 881a, Vernon's Ann.Civ.St., is applicable to the questions here presented. Sections of that Article are numbered from 1 to 69 both inclusive, and we will refer to the sections which in our opinion control our decision.

Sec. 2 provides that when a proposed charter, or articles of association, for a building and loan association has been filed if it appears to the satisfaction of the Commissioner that the minimum capital required has been paid in cash then he shall determine:

> ". . . whether the character, responsibility and general fitness of the persons named in the articles of incorporation are such as to command confidence and warrant belief that the business of the proposed building and loan association will be honestly and efficiently conducted in accordance with the intent and purpose of this Act, and whether the public convenience and advantage will be promoted by allowing such proposed building and loan association to be incorporated and engaged in business, and whether the population in the neighborhood of such place and in the surrounding country affords a reasonable promise of adequate support for the proposed building and loan association."

The Section then provides that if the Commissioner is satisfied concerning the matters above specified that he shall issue a certificate to the association which shall then become a body corporate and authorized to exercise powers not inconsistent with the provisions "of this Act." However before engaging in business by-laws must be adopted and approved by the Commissioner and the association must secure a certificate of authority to do business from the Commissioner under Section 4.

If the Commissioner is not satisfied "that it is expedient and desirable to permit such proposed building and loan association to engage in business" then under Section 3 he shall refuse the application.

Section 7 provides that the Commissioner shall have the supervision over and control of all State building and loan associations and charges him with the execution of the laws of the State relating to such associations.

Other sections provide for the making of reports to the Commissioner by associations, examinations of them by him, keeping of books and accounts by them, authorize the Commissioner to cause the correction of illegal, unauthorized, unsafe or fraudulent practices of the association on penalty of the association's certificate of authority being annulled. Other sections deal with matters not of controlling importance here.

The sections above quoted from and referred to clearly show that it was the intent of the Legislature to promote the public convenience and advantage in authorizing building and loan associations to engage in business in this State and to accomplish and insure this purpose the Commissioner was vested with the powers and the authority set out in the laws relating to these organizations and the conduct of their business.

> "It is the settled law that the constitutional and statutory laws of this state in force when a corporate charter is granted are parts of such charter, though not expressly incorporated therein." Shaw v. Lone Star Building & Loan Ass'n, 123 Tex. 373, 71 S.W.2d 863, 867.

Southwestern's charter was approved and its certificate of authority to do business was issued and both were accepted on the conditions named in the statutes. The Commissioner's action in approving the charter and issuing the certificate of authority was founded, in part at least, on his findings that the public convenience and advantage would be promoted by allowing Southwestern to engage in business at 3401 South Main Street, Houston, and that the population in that neighborhood and in the surrounding country afforded a reasonable promise of adequate support for it. In making these findings the Commissioner surveyed the designated location and was not called upon to survey locations not specified but where future public offices may be located.

It is quite evident that the Commissioner could not perform the duty of supervising and controlling Southwestern and execute the laws relating to it without being afforded the opportunity to approve or disapprove the place where it conducted business. In Von Rosenberg v. Lovett, Tex.Civ.App., 173 S.W. 508, 514, Er. ref., the Court considered the meaning of a statute which made it the official duty of the board of equalization "to supervise the assessment of their respective counties." The Court said: "To supervise does not mean to do the work in detail, but to see that it is done. It means to oversee, with power of direction." In Smithson v. Callahan, 78 U.S.App.D.C. 355, 141 F.2d 13, 14, the Court considered the meaning of "supervision" used in a local court rule requiring the trustee administering an estate under the supervision of the court to file reports, etc. The Court said that supervision "implies a duty in the trustee to consult the court before taking action." When the word "control" is placed in company with "supervision" as it is in Section 7 supra, it appears certain that the Legislature has made it the duty of the Commissioner to exercise "a directing, restraining and governing influence over" Southwestern, and that the establishment and operation of branch offices comes within such supervision and control.

It is our opinion that the Commissioner's approval must be obtained by State building and loan associations prior to the opening of additional public offices for the transaction of their business. It is also our opinion that the rules promulgated and above referred to are valid and binding from and after January 29, 1958. These rules do no more than prescribe requirements for securing the Commissioner's approval for opening additional public offices.

Southwestern says that an interpretation of Section 7 such as we have given it would make the section unconstitutional. We do not agree. The powers and privileges accruing to Southwestern are derived from constitutional and statutory provisions. Section 2 of Art. 12 of our Texas Constitution, Vernon's Ann.St., provides:

> "General laws shall be enacted providing for the creation of private corporations, and shall therein provide fully for the adequate protection of the public and of the individual stockholders."

The Legislature by enacting the provisions of law above mentioned has undertaken to comply with this mandate of our Constitution and in protecting the public and the stockholders has not violated it.

Southwestern has not, and we are unable to, place a finger on any provision of the Constitution that has been violated.

> "When a judge pronounces a law to be contrary to the constitution, he must be able to put his finger upon the provision of that instrument which prohibits the act, or from which the prohibition necessarily arises. We find in the constitution no such language, nor do we find any provision from which such

> prohibition can be fairly implied." Harris County v. Stewart, 91 Tex. 133, 41 S.W. 650, 656.

The building and loan statute (Art. 852 et seq. Vernon's Ann.Civ.St.) has been held constitutional. Standard Savings & Loan Ass'n v. Davis, Tex.Civ.App., 85 S.W.2d 333. Er. ref.

It is our opinion that the trial court was correct in denying the declaratory judgment prayed for by Southwestern and in decreeing that the promulgated rules supra were valid from and after their date. The holding of the trial court that such rules did not apply to the proposed branch offices is not disturbed. In order to support this holding of the trial court it is necessary to treat the letter above referred to as an application by Southwestern for permission to open public offices. The trial court apparently so treated the letter and we do the same. This however does not relieve Southwestern of the duty of securing the approval of the Commissioner for the opening of such public offices.

It is our further opinion that the trial court erred in granting the injunction complained of by the Commissioner, accordingly it is dissolved.

What we have said renders unnecessary a consideration of findings made by the trial court and complained of by the Commissioner.

The judgment of the trial court is in part affirmed, in part reversed and the injunction restraining the Commissioner from taking any action to prevent Southwestern from opening six proposed branch offices is dissolved.

Affirmed in part, reversed in part and injunction dissolved.

HUGHES, J., not sitting.

On Appellee's Motion for Rehearing

GRAY, Justice.

In its motion for rehearing appellee says that we erred in our original opinion and presents ten assignments. What we said in our opinion is sufficient to dispose of all these assignments except the fifth which is that we

> "erred in failing to hold that the departmental construction of the statutes was to the effect that prior approval of the Banking Commissioner was not necessary in that the evidence clearly shows that the departmental construction was to the effect that the Commissioner's prior approval was not necessary, and in that the Legislature having amended the law on numerous occasions during the time of the existence of such departmental construction did not change it, and thereby incorporated such construction into the statute."

We will however further notice appellee's argument that our construction of section 7 of Art. 881a would make the section unconstitutional.

Appellee says in its motion that:

> ". . . since the Banking Commissioner has approved the opening of these branch offices, Southwestern has a right to establish and operate said branch offices."

If this statement be correct it would appear that this court is doing a useless thing in deciding whether such approval is required. However we will here concern ourselves with the questions noted supra.

In the "Statement" in appellee's motion for rehearing, signed by the Honorable Dow H. Heard, it says:

> "Counsel for Appellee Southwestern filed on Tuesday afternoon, October 28, 1958, its 52-page Reply Brief to Brief for Appellant. The opinion of the Honorable Court of Civil Appeals was handed down early Wednesday morning, October 29, 1958, and reproduced copies thereof were mailed to the parties of record on that date. Further, on Tuesday, October 28, 1958, Appellant's Reply Brief of some 25 pages was also filed.
>
> "It struck counsel for Appellee Southwestern with some peculiarity and substantial force that the opinion of the Honorable Court of Civil Appeals was handed down so promptly after the receipt of the Reply Brief filed by Appellee."

We think it should not have required much concentrated thinking to conclude that our opinion was prepared, examined and approved prior to the filing of the reply brief and that after it was filed we did not see fit to change our decision.

This court has been most liberal in allowing parties to file briefs and replies. Here appellee's motion for rehearing was filed November 13, 1958. On November 26, it filed a "Further Exposition of Appellee's Motion for Rehearing" and on December 12 it filed its reply to appellant's reply to appellee's motion for rehearing which was filed December 3, 1958. Thus it appears that the motion for rehearing is sufficiently presented for our disposition.

In our consideration of assignment five supra we are concerned with the statutes dealing with the Commissioner's supervision and control of State chartered building and loan associations. In our original opinion we discussed sections 2 and 7 of Art. 881a. Here we will also notice Art. 342–114, Vernon's Ann.Civ.St. (cited by appellee) giving to the Building and Loan Section of the Finance Commission of Texas authority to promulgate general rules and regulations applicable to State associations.

Reference to Vernon's Annotated Civil Statutes shows that Sec. 2 supra, was enacted in 1929 by the 41st Legislature at its second called session and that it has not since been amended. Section 7, supra, was first enacted in 1929 by the same Legislature that enacted section 2. It was amended in 1939 and again in 1943 and has not since been amended. Art. 342–114 was enacted in 1943 and has not been amended. Sections 24 and 35 of Art. 881a, Acts 55th Leg., p. 1319, Chapter 445, were amended in 1957 but those sections and their amendments are not relevant to the inquiry here.

In its motion appellee says:

> "When the legislature re-enacted the statute on many occasions, or amended it in small particulars, it did so with the full knowledge of the departmental construction then in existence. Therefore, the Legislature incorporated the departmental construction into the statute itself."

Appellee argues that the Commissioner testified that in his opinion his approval was not required for the establishment of branch offices. We will concern ourselves with what the record shows has been done by the Department that may or may not constitute departmental construction of the question before us.

The present Commissioner whose testimony is referred to supra on February 6, 1952, by letter from the attorney for the Banking Department, was advised in part as follows:

> "Now, it is not a matter of discretion with you as Banking Commissioner as to allowing branch offices out of analogy. The prohibition of places of business as to banks is a fundamental or constitutional one. Whereas, the provision for the place of business for the building and loan associations is purely one of statute.
>
> "From these considerations I am of the opinion a state chartered building and loan association may have one or more branch offices at which to carry on its business, which such offices need not be mentioned by location in the articles of association."

This letter then went on to say:

> ". . . Where an association does have a branch or branches, it should report their establishment forthwith to this Department as an essential incident to its supervisory powers."

The letter concluded by stating that a "very perplexing question" might arise where the branch office in truth becomes the principal place of business "conceivably outside of the city or even county where the original principal place was located, . . ." Prior to this letter (which was after the amendments supra) no departmental construction is shown. The letter itself disputes that there was a departmental construction prior to that date. Appellee relies on this letter to establish its claimed departmental construction.

The Commissioner testified, by deposition, that after the above letter he took further steps to get advice as to his right to act on applications for branch offices for State chartered building and loan associations, and that on February 24, 1956 and November 4, 1956, he received advice from the Attorney General. These opinions were introduced in evidence and show that the advice to the Commissioner was that he should make his own investigation and determine whether the convenience and advantage of the public will or will not be served.

After the above letter of February 6, 1952 supra the Commissioner approved applications to establish branch offices at least on the following dates: March 11, 1952, which approval was cancelled by the Commissioner on October 23, 1952; March 25, 1952; April 24, 1953 and November 30, 1956.

On March 11, 1957, the Attorney General, in response to a request by the Commissioner, rendered an opinion that approval by the Department of Banking was necessary for the opening of branch offices by State chartered building and loan associations.

Appellee's point five supra cannot be sustained because there has been neither a long continued or a well settled departmental construction "to the effect that prior approval of the Banking Commissioner was not necessary" for the opening of branch offices. This being true the question of legislative re-enactment of statutes in conformity with departmental construction is not presented.

To sustain appellee's argument that there has been a departmental construction that the Commissioner's prior approval is not required for the opening of branch offices the following must appear: (1) the statute in question must be ambiguous and be susceptible of more than one construction, and (2) that the agency charged with the duty of administering it has given it a practical interpretation. If this interpretation is shown to be long continued and uniform, it is to be given weight by the courts. Texas Employers' Ins. Ass'n v. Holmes, 145 Tex. 158, 196 S.W.2d 390, 395. In any event appellee has failed to establish requirement (2). The evidence negatives interpretation by the Commissioner.

If it be argued that the failure of the Legislature to amend the applicable statutes subsequent to the letter of February, 1952, supra is legislative approval of the construction of the statutes given by that letter, then the answer to the argument is that there is no evidence in this record and no indication that the Legislature ever had the letter before it. Commissioner of Internal Revenue v. Glenshaw Glass Co., 348 U.S. 426, 431, 75 S.Ct. 473, 99 L.Ed. 483, 490, citing cases.

Our holding that section 7 of Art. 881a gives the Commissioner supervision and control of branch offices, prior approval of their location and authority to promulgate rules with reference to applications for their opening is challenged by appellee with the argument that our construction of the section renders it unconstitutional as a delegation of law making power.

In 42 Am.Jur. p. 334, Sec. 43 at page 336, it is said:

> "In considering the true test as to whether a power is strictly legislative or whether it is administrative and merely relates to the execution of the law, the true distinction is between the delegation of power to make the law, which necessarily involves a discretion as to what it shall be, and the conferring of authority or discretion as to its execution, to be exercised under and in pursuance of the law. The first cannot be done; to the latter no valid objection can be made."

Appellee does not appear to argue that the Commissioner does not have authority to promulgate rules as to the powers conferred on him by statute but says that the power of supervision and control over associations does not include the authority to require prior approval for opening branch offices, and further says that the act does not contain any standards by which such authority is to be exercised.

The rules set out the standards governing the applications and the findings to be made at the hearing. These are substantially the same as set out in section 2.

If appellee's argument was sustained the effect would be to permit an association to obtain permission from the Commissioner to open its principal office at a given location, then open a branch office at another location and proceed to conduct its principal business, or even all of its business, there. In this manner the "very perplexing question" mentioned in the letter of February, 1952, would arise and the supervision and control of the Commissioner would be defeated. In this manner the enforcement of the provisions of Art. 881a would be rendered impossible. Such a construction of the statute should not be adopted. Davis v. Estes, Tex.Com.App., 44 S.W.2d 952. Thereby building and loan associations would be enabled to defeat the purpose of the statute. Smith v. Texas Co., Tex.Com.App., 53 S.W.2d 774.

Appellee's motion for rehearing is overruled.

Motion overruled.

HUGHES, J., not sitting.

Three Year Statute of Limitations Applicable to Forgery Case

Plaintiff corporation, a depositor in the defendant bank, brought suit against the bank for paying the corporation's checks containing forged indorsements which had been placed on the checks by an employee of the corporation. The bank, in defending itself moved for a summary judgment dismissing that part of the plaintiff's claim which arose more than three years before the action was filed. The court was in effect asked to determine whether the state's general three year statute of limitations applied to this situation or whether the rights of the parties were governed by a six year statute of limitations pertaining to bills of exchange. The latter statute read as follows:

> "When a cause of action arises from a promissory note, bill of exchange, or an acknowledgment under the hand of the party of a subsisting demand, the action may be commenced at any time within 6 years from the accruing of such cause of action."

The court ruled in favor of the bank, reasoning that the 6 year statute of limitations did not apply to this action since it did not "arise" from a bill of exchange in the sense required by the statute. The statute, according to the court, applies to suits arising from the obligations directly created by the instruments themselves rather than to actions where a bill of exchange plays an important part in the factual situation. This suit was one pertaining to the contract between the corporation and the defendant bank and was thus governed by the general three year statute of limitations. *Security Storage Company v. Equitable Security Trust Company*, Superior Court of Delaware, 147 A.2d 507. The opinion of the court is as follows:

CHRISTIE, J.—Plaintiff corporation maintained a checking account at defendant bank. Plaintiff employed Samuel H. Chestnut as a claims adjustor. On several occasions over a period of years, Chestnut caused plaintiff's bookkeeper to draw checks on the defendant bank in favor

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NOTE—For similar decisions see B. L. J. Digest (Fifth Edition) § 1397.

of certain persons, ostensibly to pay for repair work to furniture in settlement of claims. Some of these checks were for actual services rendered; others were for fictitious charges fabricated by Chestnut. Chestnut endorsed the checks that had been drawn to pay fictitious bills forging the payee's signature thereon and then he added his own name below the forged endorsement. Over a period of years, the defendant bank appears to have paid Chestnut a total of $5,068 on checks containing forged endorsements. In each case, plaintiff's account was debited. This action was brought against Equitable Security Trust Company (now the Bank of Delaware) to recover the funds alleged to have been wrongfully debited to plaintiff's account as a result of such payments to Chestnut.

Defendant has moved for summary judgment as to $2,714, that portion of the claim which arose more than three years before the action was filed. The period of limitations is the only issue raised by this motion.

Defendant's motion is based upon the three year statute of limitations found in 10 Delaware Code, § 8106, which reads as follows:

> "No action to recover damages for trespass, no action to regain possession of personal chattels, no action to recover damages for the detention of personal chattels, no action to recover a debt not evidenced by a record or by an instrument under seal, no action based on a detailed statement of the mutual demands in the nature of debit and credit between parties arising out of contractual or fiduciary relations, no action based on a promise, no action based on a statute, and no action to recover damages caused by an injury unaccompanied with force or resulting indirectly from the act of the defendant shall be brought after the expiration of 3 years from the accruing of the cause of such action; subject, however, to the provisions of sections 8107–8109 and 8118 of this title."

Although section 8106 refers to several specific forms of action, it may for convenience insofar as this case is concerned, be characterized as a general statute of limitations. By its terms, the general statute of limitations is subject to the provisions of certain other sections of the Code, which set up among other things special periods of limitations as to particular types of actions or claims. Among the exceptions to the general statute of limitations is 10 Delaware Code, § 8108 which reads as follows:

> "When a cause of action arises from a promissory note, bill of exchange, or an acknowledgment under the hand of the party

of a subsisting demand, the action may be commenced at any time within 6 years from the accruing of such cause of action."

If the section 8108 applies to the claim asserted in the case before the Court, the general three year limitation would not apply and defendant's motion is without merit. If, on the other hand, section 8108 does not apply, the general limitation would apply and defendant's motion must be granted.

Since it is conceded for the purposes of this motion that a check may be regarded as a bill of exchange, the problem raised centers entirely around whether or not this action "arises from a bill of exchange" within the statutory meaning of that phrase.

There appears to be no reported Delaware case in which the Court was called upon to decide between the two periods of limitations, and the wording of corresponding statutes in other states differs from that employed in the Delaware statute.

This Court has applied the three year statute of limitations now contained in 10 Delaware Code, § 8106 to an action by a depositor against a bank for improper debits but no other period of limitations was suggested since checks were not there used in connection with the debits. Keller v. President, Directors and Company of Farmers' Bank, 1942, 2 Terry 471, 24 A.2d 539.

Plaintiff points to the very important and obvious part which checks played in Chestnut's scheme to defraud his employer. Defendant, on the other hand, argues, in effect, that actions "arise from" checks only where the parties to the checks are suing on the obligation created by the check, as for example, when the payee sues the drawer on the check because the amount of the check was not paid upon presentation to the drawee. Defendant states that this action is to recover for an alleged improper depletion of a depository account and that it is quite incidental that checks were used by a third party to trick the bank into an improper debit. Defedant's position is in essence that a suit "arises from" a check only when it is a suit upon that instrument.

Defendant quotes the following passage in support of its position:

> "The statutory description of an action as 'founded on an instrument in writing' or equivalent phrase refers to contracts, obligations, or liabilities growing, not remotely or ultimately, but immediately, out of written instruments; and the written instrument relied on must itself contain a contract to do the thing for the nonperformance of which the action is brought." 53 C.J.S. Limitations of Actions § 60.

Defendant also cites Coffin v. Fidelity-Philadelphia Trust Company, 1953, 374 Pa. 378, 97 A.2d 857, 39 A.L.R.2d 625, for the general proposition that an action against a bank to recover the amount of checks drawn upon the depositor's account on checks upon which payee's names were forged is an action based upon a contract, but not on the instrument itself. See also Railroad Building, Loan & Savings Ass'n v. Bankers' Mortgage Co., 1935, 142 Kan. 564, 51 P.2d 61, 102 A.L.R. 140. Republic National Bank of Dallas v. Maryland Casualty Co., Tex.Civ. App., 1944, 184 S.W.2d 496.

In support of plaintiff's position that this cause of action "arises from" the checks, plaintiff cites 6 Delaware Code, § 227 which provides as follows:

> "A bill of itself does not operate as an assignment of the funds in the hands of the drawee available for the payment thereof, and the drawee is not liable on the bill unless and until he accepts the same."

From this language, plaintiff concludes that defendant was not liable to plaintiff on the bills in the present case unless and until it accepted the bills. Thus, argues plaintiff, only upon acceptance of the bills did defendant become liable to plaintiff and at that time a cause of action "arises from" the bills.

This argument presumes that drawee's liability upon the bills referred to in 6 Delaware Code, § 227 may include drawee's liability to the depositor for debiting depositor's account after unauthorized payment of a bill containing a forged endorsement. A study of the negotiable instruments law and the cases decided under that section thereof shows that this interpretation is in error. Section 227 refers to drawee's liability "on the bill", that is, to his obligation to the payee or payee's order to pay the bill. See cases cited in 5 U.L.A., § 127. The section has no application to the drawee's obligations to the depositor for improper debits resulting from payments in connection with forged endorsements.

I conclude that this action is a contract action but that it is not based upon a bill of exchange. However, our six year statute of limitations does not apply to actions "based upon bills of exchange" but rather that it applies to actions which "arise from a bill of exchange." Can an action not brought upon the negotiable instrument itself nonetheless "arise from" such instrument? Or more specifically, does this action "arise from" the checks used as the term "arise from" is used in the statute of limitations even though the suit is not upon the checks?

The complaint in this case clearly relies on a bank's contractual obligations to its depositor and not upon any contract contained in the checks used by Chestnut.

Plaintiff cites the case of Union Tool Co. v. Farmers' & Merchants'

National Bank, 1923, 192 Cal. 40, 218 P. 424, 429, 28 A.L.R. 1417, as authority for the proposition that the instant case is an action "arising from" the checks bearing the forged endorsements. In that case, the Court had a factual situation roughly similar to the facts before this Court. The California Court had to decide between statutes of limitations one of which limited actions "brought to recover money deposited with any bank" and the other limited actions "by a depositor against the bank for the payment of a forged . . . check." The Court decided that the more specific language dealing with forged checks applied to the case before it. The Union Tool case holds that a specific or special statute of limitations governs those actions to which it specifically refers to the exclusion of a more general statute of limitations which would apply in the absence of the specific statute. If the language of section 8108 applies to the action before this Court, it is obvious that the limitation therein contained would apply to the exclusion of the general limitation. However, in the Union Tool case, the Court did not determine whether the suit arose from a bill of exchange since under the specific language of the California statutes, that question was not before the Court.

I am of the opinion that the passage quoted above from 53 C.J.S. Limitations of Actions § 60 correctly states the interpretation which should be given to 10 Delaware Code, § 8108.

It appears to me that the General Assembly had reference to suits arising from the obligations directly created by the instruments themselves when it used the words "arises from a bill of exchange." Such an interpretation would assign a relatively clear and easily ascertainable meaning to the statute. The other alternative is to hold that an action is deemed to "arise from a bill of exchange" if a bill of exchange played an important part in any factual situation from which the cause of action arose and even though the cause of action be based upon a contract not contained in the bill of exchange. I believe such an interpretation would be out of keeping with the usual rule, and with the probable intent of the General Assembly, and it would be uncertain and difficult to apply.

For the reasons stated, I conclude that the suit before the Court is not upon bills of exchange nor does it "arise from bills of exchange" as that term is used in 10 Delaware Code, § 8108. It follows that the six year statute of limitations contained in 10 Delaware Code, § 8108 does not apply, and the three year general statute of limitations contained in 10 Delaware Code, § 8106 does apply.

Defendant's motion for summary judgment as to that portion of the cause of action which is barred by the limitation contained in 10 Delaware Code, § 8106 is granted.

Savings Bank Ruled Liable for Negligence in Paying Over Funds

The mother of an infant son went to an officer of the defendant savings bank and explained that she wanted to open an account. She indicated that most of the funds to be placed in the account would consist of money belonging to the infant who was to receive it from his grandmother. The bank officer told the mother to open an account in her name in trust for the boy. This was done and the funds were deposited in the account. Later, although the mother attempted to keep the passbook for the account away from the infant's father, who the court characterized as "a convicted forger", the father managed to get the passbook and on two separate occasions made withdrawals of $1,400 from the account on the basis of forged withdrawal slips. Each time the father made the withdrawals he refused to take the bank's check in payment but rather insisted on cash. Apparently only a perfunctory check of his identification was made before the bank made payment.

In these circumstances the court ruled that the mother, representing the infant, could recover the funds from the bank on the ground that the bank through its employees had been negligent in making payment without exercising due care to ascertain that the father was entitled to the funds. *Bloom, Guardian ad litem, v. The Bank for Savings,* Municipal Court of the City of New York, 180 N.Y.S.2d 934. The opinion of the court is as follows:

MURRAY H. PEARLMAN, J.—The trial of the above entitled action was commenced on October 8, 1958 and thereafter continued on various dates, namely, to October 10, 1958, October 15, 1958 and October 20, 1958 and finally concluded on November 17, 1958.

This is an action to recover from the defendant The Bank for Savings the sum of twenty-eight hundred dollars paid to one Felix Bloom, the father of the infant, when he presented the passbook and two forged orders for fourteen hundred dollars each at The Bank for Savings on the 25th and 26th days of April 1957.

NOTE—For similar decisions see B. L. J. Digest (Fifth Edition) § 1362.

The account in question was opened by Shirley Bloom, mother of the infant, on November 20, 1956, after she had explained to an officer of the defendant bank that the money to be deposited belonged to the infant plaintiff and was to come from his grandmother who wanted to leave the money to him. This conversation was not denied and I find as a question of fact that it took place. The bank officer then told Mrs. Bloom to open up the account in her name in trust for the boy. Almost all of the funds that eventually came into the deposit consisted of a check received by the grandmother in an accident case, and was endorsed over to Mrs. Bloom and deposited in the account.

Mrs. Bloom lived in a four-room apartment at 2104 Caton Avenue, Brooklyn, New York. The apartment consisted of four rooms, namely, a kitchen, a living room and two bedrooms. Mrs. Bloom and her husband and son occupied one bedroom and the remaining bedroom was occupied by her father and mother. In view of the fact that her husband was a convicted forger Mrs. Bloom kept the passbook in question and another passbook in a bureau in her parents' bedroom. She had two other passbooks which she kept in a bureau of her own room because the accounts were small and most of the money had come from her husband so that she was not particularly concerned if her husband would attempt to make off with those two other passbooks. Inasmuch as the mother was bedridden and was being attended by a nurse, Mrs. Bloom placed the books for safekeeping in the bureau drawer located in her father's and mother's room. I find as a fact that there was no contributory negligence on her part that enabled her husband to obtain the book and deceive the bank. In passing, I note that Judge Finelite in Fiero v. Franklin Savings Bank, 124 Misc. 38, 207 N.Y.S. 235, 239, held that the negligence of the depositor did not "relieve the bank from its obligation to exercise care and diligence to prevent payment to the wrong person." However, in this case I have factually found that there was no negligence on the part of Mrs. Bloom.

Mrs. Bloom discovered on the morning of April 29, 1957 that the passbook in this case was missing. She rushed to the defendant bank and ascertained that two withdrawals had already been made along with a deposited check that did not clear. Each withdrawal slip was made payable to F. Bloom or bearer and signed allegedly Shirley Bloom.

A Mr. Paul Cheney, employed by the Indemnity Insurance Company of North America which was on the bond for the bank, was present in the bank at the time. Mrs. Bloom was referred to him and he promised to make good her money, if she would prosecute the forger. She took such steps but never received the money.

The two withdrawal slips were signed by signatures that were obviously not that of Shirley Bloom. After hearing the defense and observing the witnesses presented by the defendant, there is no doubt in my mind as to the negligence of the bank.

The first witness was Katherine C. Kassavian, who testified she was the assistant head teller in defendant's bank. Mr. Bloom presented her with a withdrawal slip dated April 25, 1957, which read "Pay to F. Bloom or bearer." Because he refused a check she referred the matter to an officer of the bank, as her limit of authority to pay cash was five hundred dollars. She claimed that she and an officer, who was not produced, checked the signature with the ledger and signature cards and found the signature authentic. She admitted that they did not get many transactions of this kind, not more than twenty-five a year as a rule. She testified that she customarily would ask for identification such as a driver's license or draftee's card. Testimony showed that Mr. Bloom had neither of these. She however testified that she did not know what identification the man had. As a matter of fact she actually claimed that she had no personal knowledge of the transaction. In view of the fact that the signatures were not identical, and a male having presented the draft, and having refused to take a check, and there being no satisfactory proof as to how the man was identified, I am convinced that the defendant was guilty of negligence in making this payment on April 25, 1957.

The next withdrawal on April 26, 1957, requires but little discussion. The book and the forged draft were presented to Winifred Caraher, a teller whose limitation to pay cash was one thousand dollars. Again a check was refused and she referred the transaction to Katharine C. Kassavian, the assistant head teller, because her authority as stated before was limited to one thousand dollars. No explanation was offered why she referred this transaction to Miss Kassavian who for some unknown reason had only half the authority to pay cash that Mrs. Caraher had. The negligence of the bank in connection with this transaction is obvious. Furthermore, Emil H. Karcher, the defendant's Assistant Controller, testified that each withdrawal herein "is a rare kind of transaction." He frankly admitted that he would not pay more than one hundred dollars on an identification of a driver's license and he would have made a telephone call for verification, all of which gives a clean insight as to just how negligent the employees of the bank were on both of these transactions.

I have taken the testimony of George F. Cody, and Paul N. Cheney and find their testimony to be of no value.

The rule has long been settled that a bank in making payment cannot rely solely upon the possession and presentation of the bank book or passbook. It must exercise ordinary care and diligence to ascertain that the person receiving the money is entitled to it; Kelley v. Buffalo Savings Bank, 180 N.Y. 171, 72 N.E. 995, 69 L.R.A. 317; Gearns v. Bowery

Savings Bank, 135 N.Y. 557, 32 N.E. 249; Kummel v. Germania Savings Bank, 127 N.Y. 488, 28 N.E. 398, 13 L.R.A. 786; Gerardi v. New York Savings Bank, 58 Misc. 183, 109 N.Y.S. 22. I find that no such care was exercised herein. In the instant case which makes it stronger, the bank was informed in advance that the money belonged to the infant plaintiff, and the male applied for the withdrawal, and not the female who made the deposit. Greater attention should have been paid to this "rare kind of transaction" and this situation comes directly under the authority of Ficken v. Emigrants' Industrial Savings Bank, 33 Misc. 92, 67 N.Y.S. 143.

An additional defense has been raised that the plaintiff is not the real party in interest as title to the account was in the name of Shirley Bloom in trust for the infant and that she alone could bring the action. Defendant has cited Matter of Totten, 179 N.Y. 112, 71 N.E. 748, 70 L.R.A. 711, as its authority. In Matter of Totten, the opinion of Vann, J., contained the following, 179 N.Y. at page 125, 71 N.E. at page 752:

> ". . . a deposit by one person *of his own money* in his own name as trustee for another, standing alone, does not establish an irrevocable trust during the lifetime of the depositor. . . ." (Emphasis mine.)

Here the proof is clear and I make a finding of fact that the monies deposited belong to the infant plaintiff and not to Shirley Bloom and were a gift to him from his grandmother. Therefore the Totten case does not apply at all.

In the case of Hodgins v. Zabel, 7 Misc.2d 484, 166 N.Y.S.2d 135, 136, plaintiff sued his daughter to obtain the contents of a bank account. The account was in the name of the daughter in trust for the father. The opinion of Bonparth, J. contained the following:

> "The form of the deposit is not conclusive, both parties named in the account being still alive. And as between the persons named in the deposit, any presumption arising from the form of the deposit or account may be overcome by proof, as to the true nature of the transaction. In re Porianda's Estate, 256 N.Y. 423, 425, 176 N.E. 826; Matter of Bolin, 136 N.Y. 177, 180, 32 N.E. 626; Moskowitz v. Marrow, 251 N.Y. 380, 397, 167 N.E. 506, 511, 66 A.L.R. 870; Morris v. Sheehan, 234 N.Y. 366, 138 N.E. 23."

In the instant case the undisputed proof was that the bank official who opened the account knew that the monies belonged to the infant plaintiff and if he opened the wrong kind of an account, the bank alone was at fault and is estopped from denying that the title to the account was in the infant plaintiff. As was recently said by our Court of Appeals, "an estoppel . . . 'rests upon the word or deed of one party upon which another rightfully relies, and, so relying, changes his position to his injury' . . .". Triple Cities Construction Co. v. Maryland Casualty Co., 4 N.Y.2d 443, 176 N.Y.S.2d 292, 295. There is overwhelming proof that the plaintiff is entitled to judgment.

Accordingly, I direct judgment for the infant plaintiff in the sum of twenty-eight hundred dollars together with interest and costs from the 29th day of April, 1957.

INTERNAL REVENUE SERVICE MAY NOT REQUIRE FOREIGN BANK RECORDS

Application of First National City Bank of New York,
United States District Court, 166 F. Supp. 21

The records of a foreign branch bank are not subject to production under summons by the Internal Revenue Service according to a recent ruling of a United States District Court. Immunity from such action by the tax authorities is found in a portion of the United States Code which indicates that: ". . . every national banking association operating foreign branches shall conduct the accounts of each foreign branch independently of the accounts . . . of its home office." *For similar decisions see B.L.J. Digest (Fifth Edition)* § 215.

Makers of Note Fail to Prove Defense

One of the most common cases appearing before the courts nowadays involves the situation where a contractor who is supposed to install storm windows or asbestos siding or do similar work on residences, does not adequately perform. The contractor discounts the home owner's note with a bank and the bank must ultimately bring suit against the owner who refuses payment on the ground that the contractor did not complete his contract or that the product was not as represented.

In a recent Connecticut case, this general situation occurred with a contractor who had installed aluminum storm windows unsatisfactorily. When the bank sued the makers of the note, they alleged that the contractor had obtained their signatures by fraud, representing that their signatures on a blank note were to be used to determine their credit. The court ruled that the makers not only had to allege this defense, but also to prove it before the bank, as holder of the note, had the burden of going forward to prove that it was a holder in due course.

The makers had not been able to prove fraud in the execution of the note and the court in ruling for the bank, found that it was a holder in due course. *First National Bank & Trust Company of New Haven v. Roehl et al.*, Supreme Court of Errors of Connecticut, 148 A.2d 257. The opinion of the court is as follows:

MURPHY, A.J.—In March, 1955, the First National Bank and Trust Company of New Haven, hereinafter referred to as the bank, brought suit against Herbert C. Roehl, Sr., and his wife, Mae F. Roehl, to recover the face amount of a note for $825.48 dated December 27, 1954, plus attorney's fees as provided in the note. In November, 1956, the Roehls instituted an action against Paul Ambeltsiotis, the payee of the note upon which the bank had sued. From the manner in which this complaint has been drafted, it is extremely difficult to determine the nature of the cause of action. We will consider it, as the court below apparently did, as an attempt to allege wrongful completion and negotiation of the note and failure by Ambeltsiotis to carry out an agreement entered into when the action upon the note was originally reached for trial on November 22, 1955. The trial court rendered judgment

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NOTE—For similar decisions see B. L. J. Digest (Fifth Edition) § 660.

against the Roehls in both cases and they have appealed.

The facts in these cases are these: On November 21, 1954, Ambeltsiotis was a distributor of aluminum windows and doors in New Haven, doing business as the Stormaster Window Company. Two of his employees were John A. Frederick, an installer, and William Merico, a salesman. Frederick was then a prospective son-in-law of the Roehls. He has since married their daughter. Mr. Roehl was the owner of the family home at 279 Lenox Street, New Haven. At his request, Frederick had arranged to purchase, for him, thirty-two storm windows and a door with a grille from Ambeltsiotis at dealers' prices, the installation to be made by Frederick. Merico demonstrated the windows to the Roehls and made the necessary measurements as a favor to Frederick. On November 21, Merico filled out, and Roehl signed, a contract to purchase the windows and door for $697.83. Roehl also filled out and signed an application to the bank for a property improvement loan. It contained pertinent information concerning his financial condition. Subsequently, the windows were delivered and Mrs. Roehl signed a borrower's completion certificate which recited that all of the articles had been furnished and installed and that the work had been satisfactorily completed. On December 27, 1954, the bank discounted a note for $825.48 made payable to Ambeltsiotis in monthly instalments of $22.93 on the tenth of each month starting February 10, 1955. The note bore the admitted signatures of Mr. and Mrs. Roehl as makers. It was indorsed on the reverse side by Ambeltsiotis, who received the $697.83 purchase price from the bank. The $127.65 difference between the amount of the note and the purchase price represents interest on the loan and insurance on the life of Mr. Roehl. On December 28, 1954, the bank mailed to the Roehls a notice, which they received, of the amount owed, together with a coupon book for the payment of the instalments. The Roehls made no payments on the note because they claimed, and the court has found, that twenty-one of the windows do not fit and the door has never been delivered.

In the suit by the bank on the note, the Roehls alleged by way of defense that the note had been signed by them in blank on representation that it, together with another paper, would be used solely to determine their credit, and that Ambeltsiotis had fraudulently obtained their signatures and negotiated the note. The defendants not only had to allege but also to prove these facts before the plaintiff had the burden of going forward to prove that it was a holder in due course and not subject to these defenses. Rev.1949, § 6351 (Rev. 1958, § 39–60); Garris v. Calechman, 118 Conn. 112, 115, 170 A. 789; Filosi v. Crossman, 111 Conn. 178, 182, 149 A. 774. An issue of fact was presented for determination by the trier. Hartford National Bank & Trust Co. v. Credenza, 119 Conn. 368, 372, 177 A. 132. That the Roehls failed to prove their allegations is apparent from the court's conclusion that there was no fraud practiced in the execution of the note. The court did not find, as it should have, that the bank was a holder in due course under the provisions of § 6344 of the 1949 Revision (Rev. 1958, § 39–53). It did conclude that the bank was the owner of the promissory note signed by the defendants. We construe this as meaning that the bank was a holder in due course. Garris v. Calechman, supra.

In the second case, the Roehls did not sue Ambeltsiotis for breach of the contract of sale. They relied upon an alleged stipulation entered into by the bank and the Roehls when the first case was reached for trial on November 22, 1955. Ambeltsiotis was not a party to that suit, was not in court at that time and did not enter into the stipulation. Under the facts and the pleadings, there was no error in excluding the statements of alleged agents of Ambeltsiotis in the absence of proof of their agency. Bailey v. Bobecki, 117 Conn. 653, 654, 166 A. 677; Metropolitan Cleaners & Dyers, Inc. v. Tondola, 114 Conn. 244, 246, 158 A. 240. The conclusion that the Roehls had failed to prove a case against Ambeltsiotis under the allegations of the complaint was fully warranted.

There is no error in either case.

In this opinion the other Judges concurred.

DELIVERY OF CHECK DOES NOT CONSTITUTE GIFT

Dailey v. Adams, 319 S.W.2d 34, Supreme Court of Arkansas

The Supreme Court of Arkansas has ruled that where a check was drawn to the order of a named payee and the check contained on its face a notation that it was payable "from my estate as mentioned in letter", the check did not operate to effect a gift upon the death of the drawer. There was no *inter vivos* gift because the payee could not cash the check at the time of delivery and until his death the drawer could revoke the transaction.

Twenty-Three Day Delay by Collecting Bank Does Not Give Rise to Recovery

A brief decision by the Appellate Division of the New York Supreme Court indicates that where a bank receives checks for collection and does not send notice of protest and non-payment for twenty-three days, the bank is not liable for negligence if no indorsers have been released and if no proof is submitted that the drawer had since become insolvent or unamenable to the process of court. *Hoffower v. Pennsylvania Exchange Bank*, Supreme Court of New York, Appellate Division, 183 N.Y.S.2d 620. The opinion of the court is as follows:

PER CURIAM.

Plaintiff partnership is the holder and payee of four checks drawn upon the defendant bank and forwarded through banking channels to defendant bank for collection with direction "to protest and wire non-payment". The defendant bank sent notice of protest and non-payment as to two of the checks twenty-three days after receipt of the same, and as to the other two checks, twenty-two days after the receipt thereof. The plaintiff brought an action in negligence against the bank and has recovered judgment for the face amount of the checks. The record does not support the finding that plaintiff's damage is the face amount of the checks. It has not lost any right of action against the drawer—there are no endorsers who have been released, and for all that appears in the record, plaintiff is in the same situation it would have been in had the bank given earlier notice of non-payment. There is no proof that the drawer of the checks has since become insolvent or unamenable to the process of the court. "The plaintiff is entitled to indemnity, and no more, for the loss caused by the fault of the defendant, and it must show the extent of such loss". First Nat. Bank v. Fourth Nat. Bank, 77 N.Y. 320, 330; see also same case, 89 N.Y. 412, 413. Since the judgment must be reversed for the error as to damages, we do not pass upon any other question.

Judgment reversed on the law and facts and a new trial granted, with costs to the appellant to abide the event.

All concur.

NOTE—For similar decisions see B. L. J. Digest (Fifth Edition) § 297.

FEDERAL BANKING LAWS

By F. GLOYD AWALT of the Washington, D. C. Bar

Notes from Washington pertaining to federal banking legislation and the regulation of banks by supervisory agencies.

Legislation

S. 57, a bill to be known as the Housing Act of 1949, was passed by the Senate on February 5, and an amended version of the bill was passed by the House on May 21. The House version of the bill is more liberal, but it requires that the funds must be authorized by Congressional appropriations committees. Both the Senate and the House versions of the bill add a new subsection (j) to section 203 of the National Housing Act which provides that mortgage loans insured under that section shall not be taken into account in applying the existing limitations (contained in sec. 24 of the Federal Reserve Act) on the total amount of real estate loans which a national bank may make in relation to its capital and surplus or its time and savings deposit. Both versions also seek to amend Title V of the Housing Act of 1949 by adding at the end thereof a new section. Subsection (a) of this new section would establish a new program under which the Secretary of Agriculture would insure loans made by private lenders to farmers, associations of farmers, and county governments for the purpose of providing housing and related structures for migratory farm labors. Such loans would have to meet the conditions applicable to direct farm housing loans by the Secretary, except that the maximum loan-to-value ratio would be 90 percent and the maximum interest rate would be 6 percent. Subsection (b) of this new section amends section 24 of the Federal Reserve Act to permit national banks to participate in the new insurance program established by subsection (a). It exempts loans insured under the new program from the limits prescribed by section 24 for loan-to-value ratios and maturities of real estate loans made by national banks. The bill is now in conference.

S. 1062, the bill to amend the Federal Deposit Insurance Act to provide safeguards against mergers and consolidations of banks which might lessen competition unduly or tend unduly to create a monopoly in the field of banking, and S. 1120, a bill to amend the National Bank Act and the Federal Reserve Act with respect to the reserves required to be maintained by member banks of the Federal Reserve System against deposits and to eliminate the classification "central reserve city," have both passed the Senate.

The House has now reported out an amended version of S. 1120. The bill as reported by the Banking and Currency Committee of the House eliminates an amendment in the Senate-passed version of the bill which seeks to amend the law with respect to reserves required to be maintained by holding companies.

As of this writing, the House Committee has as yet taken no action on S. 1062.

Subcommittee No. 2 of the House Committee on Banking and Currency has concluded hearings on H.R. 6092, to amend the lending and borrowing limitations applicable to national banks and to authorize the appointment of two additional Deputy Comptrollers of the Currency, and H. R. 6093, to amend the national banking laws to clarify or eliminate ambiguities and to repeal certain laws which have become obsolete.

Several bills have been introduced which seek to enlarge the power and scope of federal credit unions. A subcommittee of the House Committee on Banking and Currency has reported H. R. 5777, with amendments, to the full Committee. As introduced, the bill makes some changes in the organizational setup of federal credit unions; provides that members and individuals eligible to become members may be charged a reasonable fee for cashing or selling checks; increases to $1,000 the amount which may be loaned to an individual on an unsecured loan, still subject to the 10% limitation on the federal credit union's paid-in and unimpaired capital and surplus, whichever is greater; and makes provision for conversion from federal to state credit union and from state to federal credit union.

Mr. Spence has introduced a bill, H. R. 7244, to promote and preserve local management of savings and loan associations by protecting them against encroachment by holding companies.

Board of Governors of the Federal Reserve System

Reports of indebtedness of executive officers under revolving personal loan accounts. The opinion of the Board of Governors has been requested as to the type of reports which are required of executive officers of member banks who avail themselves of a form of credit described as certain revolving personal loan programs operated by a number of banks. The Board has taken the position that if an executive officer of a member bank who has been approved for credit under such a bank-financed charge plan makes a written report to the directors of his bank within ten days after approval of such credit, stating the nature and purpose of the credit, the maximum amount thereof, and the period allowed for repayment, such report will be considered to be in compliance with the requirements of the Act, and that no additional reports would be required unless the maximum amount originally approved is increased or the credit actually extended exceeds that amount.

Credit by brokers, dealers and members of national securities exchanges. Regulation T prescribes the conditions upon which credit may be extended and maintained by brokers, dealers and members of national securities exchanges. Effective June 15, 1959, the Board has adopted certain amendments to Regulation T in order more effectively to prevent the excessive use of credit for purchasing or carrying securities. The amendment to section 3(b)(2) of Regulation T provides for a new method of limiting withdrawals from "restricted" accounts. The amendment provides for a separate figure which represents the "retention requirement" of a registered non-exempted security (i.e., in the case of a withdrawal of securities, the percentage of market value that must be deposited in the account; or, in the case of a sale, the percentage of sale proceeds that must be left in the account). In a new paragraph (c) of section 8 (the Supplement to Regulation T) the "retention requirement" is set at 50 per cent of the market value of the securities involved. This "retention requirement" may be changed by the Board from time to time.

Loans by banks for the purpose of purchasing or carrying registered stocks. Effective June 15, 1959, the Board has adopted certain amendments to Regulation U in order more effectively to prevent the excessive use of credit for purchasing or carrying securities. Specifically these amendments will: (1) Amend the third paragraph of section 1 in order further to restrict withdrawals of collateral against so-called "restricted" loans (i.e., stock-collateralled loans which are larger than would be permitted in the case of a new loan to purchase registered stocks under current margin requirements); (2) strengthen the provisions of section 3(a) regarding statements accepted by a bank as to the purpose of a loan; (3) broaden the provisions relating to "carrying" in section 3(b)(1); (4) provide for reports from certain nonbank lenders by amending section 3(j); (5) prohibit, in section 3(n), the weakening of collateral behind a "purpose" loan which occurs when the same collateral is also used as the basis of a "non-purpose" loan; (6) add a new section 3(q) to require that bank loans to borrowers importantly engaged in relending for stock market purposes shall comply with this part, even though the bank loans are not secured by any stock; and (7) add a new section 3(r) to require loans originally for the purchase of convertible securities to be brought into conformity with the margin requirements within 30 days after conversion into a registered stock takes place. The amendments also make conforming changes at several places in the regulation.

On May 29 the Federal Reserve Board gave approval for a rise in the discount rate to 3½% from 3% in New York, Chicago, Dallas, St. Louis and Minneapolis.

BANKING BRIEFS

Digest of current decisions in the field of trust receipts, conditional sales, chattel mortgages and other secured transactions

Dealer Liable For Conversion of Mortgage Assignee's Interest

Universal C.I.T. Corporation v. Courtesy Motors, Inc., Utah Supreme Court, January 2, 1959

Where a mortgagor sold a motor vehicle to a dealer using a bill of sale which had the bottom part concerning liens cut off and where the dealer had actual knowledge of the mortgage but obtained a certificate of title indicating there were no liens on the vehicle which was then sold to a third person, the dealer was liable to the holder of the mortgage for conversion. *For similar decisions see B.L.J. Digest (Fifth Edition)* § 884.

Instrument Held To Be Conditional Sale Agreement Rather Than Rental Contract

First National Bank of Fort Smith v. Phillips, United States Court of Appeals, Fifth Circuit, December 11, 1958

A so called lessor was not entitled to recover chattels covered by a rental-purchase agreement upon the lessee's bankruptcy because the instrument covering the transaction was in fact a conditional sale contract rather than a rental agreement since it required the lessee to pay a purchase price and obligated the lessor to deliver a bill of sale covering the property when the instrument was paid in full. *For similar decisions see B.L.J. Digest (Fifth Edition)* § 1357.5.

Minor Permitted To Recover From Assignee of Mortgage

Poli v. National Bank of Detroit, Michigan Supreme Court, January 12, 1959

A minor may recover the value of a mortgaged motor vehicle from the assignee of a mortgage where the minor had executed the mortgage and then defaulted, since the minor had the right to resist the enforcement of the mortgage during his minority. *For similar decisions see B.L.J. Digest (Fifth Edition)* § 362.

Rescission of Conditional Sale Permitted

Bratta v. Caruso Car Company, Inc., California District Court of Appeal, Second District, December 31, 1958

Where a conditional sale contract indicated a $300 cash down payment had been made when in fact this amount was included in the unpaid balance due under the contract, the conditional buyer was entitled to rescind the sale because the instrument violated the state statute governing the contents of conditional sale contracts. *For similar decisions see B.L.J. Digest (Fifth Edition)* § 1357.5.

Recent Articles Concerning Secured Credit Transactions

The following articles are recommended reading in the field of secured credit transactions:

Security Interests in Crops. Milo Whitney Smith. 10 Hastings Law Journal, August 1958, p. 23.

Finance Companies as Holders in Due Course of Consumer Paper. William C. Jones. Washington University Law Quarterly, April 1958.

Secured Financing in Today's Bankruptcy Proceedings. Max Schwartz. National Association of Referees in Bankruptcy Journal. January and April, 1959.

BANKING LEGISLATIVE TRENDS IN THE STATES

New legislative and regulatory developments affecting small loan and finance companies, credit insurance, banking and related fields, as reported from state capitals and municipalities throughout the country, include the following:

ALABAMA: A proposed new small loan regulatory law was endorsed by the Alabama state legislative interim committee on revision of laws, which recommended that it be enacted by the state legislative session convening in May.

Drafted by a subcommittee after a series of hearings, the bill would apply only to companies lending up to $500. It proposes a rate schedule as follows:

On any loan not exceeding $500, a rate of 3 per cent on that part of the unpaid principal balance not in excess of $100; 2 per cent a month on that part of the unpaid principal in excess of $100 and not exceeding $300; and 1 per cent a month on the unpaid balance in excess of $300.

In addition to the interest rate schedule, the bill also authorizes money lenders to make a service charge of not more than $2 for loans not in excess of $24.99 and a charge of not more than $3 on loans of $25 or more.

The measure further specifies that a service charge shall not be collected on second or further loans to the same person if the loans are made within three months from the date of termination of a prior transaction.

Exempted from provisions of the bill would be banks, advances to tenant farmers, installment buying and savings and loan associations.

Penalty for violation of any provision of the measure would be a maximum fine of $500 and/or imprisonment for not more than six months.

Applications for licenses for small loan firms would be submitted to the Bureau of Small Loans, State Banking Department. They would have to be accompanied by a $100 investigation fee. The license fee itself would be $200 a year. Each license issued would cover only one place of business, but the supervisor could issue additional licenses to the same licensee upon compliance with all provisions of the act.

Under the bill, the supervisor would be empowered to revoke licenses for certain specified reasons, including "using unreasonable collection tactics."

Examination of licensees would be authorized at least once a year, with the licensee required to pay all costs of the examination.

Among other powers, the supervisor would be authorized to issue "cease and desist" orders in instances where he has "probable cause" to believe any person is violating or is threatening to violate any provision of the act.

CALIFORNIA: A bill to regulate installment sales of commodities other than automobiles was passed by the California Senate and returned to the House for concurrence in amendments before going for signature to Governor Brown, who had advocated such legislation.

The measure will limit credit charges to a maximum of $10 per $100 on the first $1,000 of a contract and $8 per $100 on amounts in excess of $1,000; require a full disclosure in print of all details of the contract and that a copy be furnished to the purchaser; and outlaw fine print clauses and prohibit blank spaces in contracts.

It also will grant the buyer the right to pay off the contract at any time and receive a rebate on the financing charge; outlaw wage attachments for a period of 60 days after the contract is in default; and entitle the buyer to attorney's fees if he is the winner in a dispute over terms of the contract.

The Senate amended the bill to extend its provisions to cover home improvement loans. It was introduced by Assemblyman Jesse M. Unruh of Los Angeles County following a two year interim study by an Assembly subcommittee he headed.

"This bill," Unruh asserted as it cleared the Senate, "will provide adequate and equitable controls over literally billions of dollars worth of installment buying contracts. It will eliminate practices discovered by our subcommittee which sometimes resulted in credit charges in excess of 300 per cent of the original purchase price of an item or service.

"It will drive the racketeers who have been waxing rich at the expense of unsuspecting consumers out of business. It will insure that no family need be stripped of all its belongings simply because one of its members was tricked by the fine print in an installment credit contract."

In explaining when the bill was originally introduced why its terms were not drafted to apply to automobile time sales contracts, Unruh had said the inclusion of provisions covering such contracts would have aroused opposition which could have killed the bill. He suggested that the subject of automobile time sales be explored further.

FLORIDA:—Killed in a Florida Senate committee was a bill which would have specified that any real estate mortgage carrying an interest rate higher than 10 per cent would be null and void.

The rejected proposal would have had the effect of exempting real estate mortgages from the securities small loan companies can demand for loans carrying interest rates up to 36 per cent per year.

Although 10 per cent now is the legal limit in Florida that a regular mortgage company can charge, the state's 1957 small loan regulatory act provides that small loan firms can take "any security mutually acceptable to both the borrower and the lender." This has been interpreted as including mortgages on real estate.

MARYLAND: Rejected in the Maryland legislature was a bill which would have allowed loan companies to increase interest rates from 6 to 8 per cent and service fees from $20 to $50 on secured loans of up to $1,500.

MINNESOTA: A bill given final passage by the Minnesota legislature and sent to the governor for signature raises the ceiling on small loans and reduces interest rates.

In the compromise form given final approval, the measure boosts the small loan ceiling from $300 to $600 and cuts the interest rate from 3 to 2¾ per cent per month on the first $300. The rate is fixed at 1½ per cent a month on amounts exceeding $300.

The measure was amended prior to enactment to further provide that total cost of the loan shall be listed in simple language in the contract.

MISSOURI: A bill to regulate installment sales of consumer goods other than automobiles and the service fee on revolving charge accounts was given initial approval by the Missouri Senate.

Senator William Baxter Waters of Liberty explained the proposal would place a ceiling on financing charges and require full disclosure to buyers of all fees in connection with installment purchases. Sellers could not require the buyer to purchase insurance beyond the amount necessary to cover the transaction.

Under the measure, which had not at this writing been acted upon by the House, the installment charge ceiling would be $12 annually on each $100 to $300; $10 on each $100 from $300 to $1,000; and $8 on each $100 above $1,000.

On revolving charge accounts, retail stores could charge 1½ cents a month on each $1 up to $500. On unpaid balances above $500, the maximum fee would be three-fourths of 1 cent on each dollar.

Senator Floyd R. Gibson of Independence offered an amendment stating that if the revolving charge provision was found to be unconstitutional the remainder of the bill would stand.

A similar bill regulating time sales of automobiles was passed earlier by the Missouri Senate and sent to the House.

NEVADA: An opinion handed down by the Nevada attorney general's office held that a Nevada license could not be issued to a Milwaukee, Wis., insurance company specializing in insuring creditors against loss should debtors fail to pay.

Written by Chief Deputy Attorney General D. W. Priest, the opinion said there is no provision in Nevada law for classifying such a company. In applying for the license, the firm described itself as a company insuring firms which make real estate loans against loss if borrowers failed to meet obligations. It admitted it was in a relatively new insurance field and suggested possible classification as a casualty, fidelity and surety insurance carrier.

Priest held that this would bypass legislative intent in the setting up of insurance classification categories.

OREGON: A bill to permit lenders to charge 12 per cent interest a year on business loans to corporations was given final passage by the Oregon legislature and sent to the governor for signature. It would permit such exceptions to the state's usury statute, setting the maximum legal rate of interest at 10 per cent.

RHODE ISLAND: A resolution proposing the creation of a legislative commission to study the state's usury laws was introduced in the Rhode Island legislature by Senate Minority Leader James H. Donnelly, North Kingston Republican.

The proposed study group would make recommendations for "a complete and up to date" revision of the interest and usury laws.

Meanwhile two banking bills were introduced in the legislature by Representatives Raymond L. Davignon, Pawtucket Democrat, and E. Louise Stoddard, Providence Republican.

One of these measures would extend from 18 to 36 months the maximum period for repaying short-term notes and would raise from $1,000 to $3,000 the maximum amount which could be obtained by an individual in short term notes from any one bank.

The other would raise the amount of investments in mortgage loans on real estate that may be made by financial institutions from 75 to 80 per cent of deposits.

TEXAS: A proposed state constitutional amendment to remove a present interest rate limitation of 10 per cent per annum and empower the state legislature to fix small loan interest rate maximums was approved by the Texas Senate after having been passed earlier by the House.

Under the measure, which would be submitted to the electorate, the legislature also would be given the power to classify loans and lenders; license and regulate lenders, and define interest. In the absence of legislation fixing maximum rates of interest, all loan contracts for a greater rate of interest than 10 per cent would be deemed usurious.

In another development, a substitute small loan regulatory bill was favorably reported to the Texas House by its banks and banking committee. The proposal combined features of House Bill No. 58, sponsored by Rep. Criss Cole of Houston on the basis of recommendations by the State Legislative Council; a variation of the council bill sponsored by Rep. Don Kennard of Fort Worth; and HB 550, sponsored by Rep. Reagan Huffman of Marshall, with the backing of many small loan firms.

The substitute bill would classify small lenders as those lending under $100 and those lending from $100 to $3,000. It would put each class under strict regulation by the state banking commissioner. Each class would be licensed and neither class could be licensed in the other class.

The banking commission would be empowered to study what the legal interest rate should be and—if the separately proposed small loan regulatory state constitutional amendment is adopted—could recommend to the legislature a more realistic maximum rate than the present constitutional limit of 10 per cent.

Meanwhile, the substitute bill would fix limits on the "gross rate of charge" for lending money in each class of small loan. This gross rate of charge would include interest, fees, brokerage and other charges.

The substitute bill would prescribe a scale of ceilings on gross rates of charge for loans from $100 to $3,000. The gross rate would be 36 per cent a year on that part of the unpaid principal balance up to $300; 24 per cent a year on that part in excess of $300 but not exceeding $600; 12 per cent a year on that part in excess of $600 but not exceeding $1,000, and 10 per cent a year on that part over $1,000.

For loans under $100, the substitute bill would fix a schedule of gross rates of charge which would allow a charge of $2.05 a month on a $50 loan and $2.30 a month on a loan of $99.99.

VERMONT: What was described as a "uniform" credit insurance regulatory bill was passed by the Vermont Senate and sent to the House.

TRUST AND ESTATE TAX DECISIONS

Digest of current decisions pertaining to the law of taxes on trusts, estates and gifts.

Closely Held Stock Valued at Option Price

Gibbs v. Commissioner of Internal Revenue, Tax Court of the United States, February 27, 1959

A husband and wife gave their son stock in a closely held corporation. At the time of the gifts the son was Secretary-Treasurer and a director of the corporation and held enforceable options to purchase 143 shares of stock at $1,100 per share. For gift tax purposes the Commissioner of Internal Revenue valued the stock at $2,500 per share, based on book value and considerable corporate earnings for the year of the gifts and immediately preceding years. The donor parents argued for a lower valuation on the basis of the corporation's erratic earnings history, the failure to pay dividends, lack of working capital and the sales price of the stock in previous and later years. *Held*: The stock had a value of $1,100 per share on the date of the gifts.

Relevant Factors in Determining Value of Closely Held Stock

Revenue Ruling 59-60, I.R.B. 1959-9, p. 8

The above Ruling has been issued "to review in general the approach, method and factors to be considered in valuing shares of the capital stock of closely held corporations for estate and gift tax purposes. The methods discussed herein will apply likewise to the valuation of corporate stocks on which market quotations are either unavailable or are of such scarcity that they do not reflect the fair market value." The Ruling lists the following factors as relevant to a determination of fair market value: "(a) The nature of the business and history of the enterprise from its inception. (b) The economic outlook in general and the condition and outlook of the specific industry in particular. (c) The book value of the stock and the financial condition of the business. (d) The earning capacity of the company. (e) The dividend-paying capacity. (f) Whether or not the enterprise has good will or other intangible value. (g) Sales of the stock and the size of the block of stock to be valued. (h) The market price of stocks of corporations engaged in the same or a similar line of business having their stocks actively traded in a free and open market, either on an exchange or over-the-counter."

Power in Settlor-Trustee to Shift Economic Benefits Between Life Tenants and Remaindermen Makes Trust Includible in His Gross Estate

State Street Trust Company v. United States of America, United States Court of Appeals, First Circuit, January 23, 1959

A father established three irrevocable trusts for his children, naming himself and a bank as co-trustees. The trustees were authorized in their discretion to invade principal for the support, comfort or maintenance of the beneficiaries. They were also authorized to exchange trust property for other property; to invest in "securities or properties although of a kind or in an amount which ordinarily would not be considered suitable for a trust investment, including, but without restriction, investments that yield a high rate of income or no income at all and wasting investments;" to determine what should be credited to income and what to principal, including all receipts resulting from ownership of stock; and to decide whether deductions for depreciation, amortization or waste should be from principal or income. The trustees were to be liable "only for their own wilful acts or defaults, but in no case for acts in error of judgment." In an estate tax proceeding, *Held*: "Perhaps no single power conferred by the [settlor father] on the trustees would be enough to warrant inclusion of the corpora of the trusts in his estate. But we believe that the powers conferred on the trustees, considered as a whole, are so broad and all inclusive that within any limits a Massachusetts court of equity could rationally impose, the trustees, within the scope of their discretionary powers, could very substantially shift the economic benefits of the trusts between the life tenants and the remaindermen. We therefore conclude that under the trusts the [father] as long as he lived, in substance and effect and in a very real sense, in the language of § 811 (c) (B) (ii), 'retained for his life . . . the right . . . to designate the person who shall possess or enjoy the property or the income therefrom;' . . . [Accordingly], the corpora of the trusts is includible in the decedent's gross estate."

Comment: Chief Judge Magruder of the First Circuit Court of Appeals dissented from the two-man majority opinion and reserved the right to file a dissenting memorandum at a later date. His dissent and any proceedings on appeal will be reported in *The Banking Law Journal*. The *State Street Trust Company* decision is extremely important to all legal draftsmen, advisors in estate planning, corporate fiduciaries and settlors of existing trusts. Unless the majority decision is reversed on appeal, it undoubtedly will become the basis for attempts by the Internal Revenue Service to include in taxable estates a great deal of trust property heretofore considered excludible. Service will certainly scrutinize trusts carefully hereafter for powers in settlor-trustees to substitute trust property. It is difficult, of course, to gauge the probable scope and significance of a decision based on extraordinarily broad trust powers "considered as a whole." Each trust will have to be reviewed in its own context, on the basis of its particular trust powers and in the light of existing State law. In one known instance, however, Service is presently seeking to include in a decedent-settlor's taxable estate the value of inter vivos trusts which provide that the "trust estate may be retained in the form in which it now is, or from time to time . . . the securities, or other investments . . . may, in the absolute discretion of said Trustees . . . be sold . . . upon such terms as said Trustees . . . may deem meet, and be thereafter held in cash or reinvested in any manner in the said absolute discretion of said Trustees . . . without reference to, or limitation by any law prescribing the investments in which trust funds may be invested."

Annual Gift Tax Exclusion Allowed Where Trustee Required to Act as if a Guardian

Revenue Ruling 59-78, I.R.B. 1959-10, p. 44

A gift was made in trust for the benefit of a minor. The trust instrument provided that trust income and principal should be used for the support, education and benefit of the minor in such manner and amounts, and at such times, as satisfied the needs and best interest of the minor, as if the trustee held the property as guardian of the minor. Trust property not used for such purposes during minority was to be distributed to the minor at age 21, or to his estate if he died before reaching 21. The above Ruling states that "a gift in trust for a minor under terms requiring the trustee to use the property for the benefit of the donee as if held by him as guardian for the donee constitutes a gift of a present interest and is, therefore, entitled to the [federal gift tax annual exclusion] of the Internal Revenue Code of 1939."

Date of "Payment" of Estate Tax

Hill and Hill v. United States of America, United States Court of Appeals, Third Circuit, February 25, 1959

Decedent died October 6, 1948. His executors filed an estate tax return on January 13, 1950, which was stamped "Paid January 18, 1950." On January 5, 1954 the executors filed a claim for refund because of failure to include a debt of decedent's as a deduction in Schedule K of the return. *Held*: "If what the [executors] did when they made their return and enclosed their check on January 13, 1950 was 'payment,' then quite obviously they have not complied with the [three year refund] time limit set by the statute. We think that what they did was payment and whether the payment took place when they mailed the check or when the Collector received it is immaterial to this case. . . . The difference, then, is whether a taxpayer gives the Government money in discharge of his tax debt or gives it money to stop interest and penalties while he and the Government contest what the debt is to be. We do not have any doubt that in the ordinary case where a taxpayer fills out his form, makes out his check and sends them in that he intends the remittance to be in discharge of his liability and that the Collector receives it in the same way."

Power to Distribute in Whole or Part Held a Taxable Power to Alter, Amend or Revoke

The Michigan Trust Company v. Kavanagh, United States District Court, Western District of Michigan, March 11, 1959

A father created three identical irrevocable trusts for his minor sons. He gave himself, as trustee, the power in his absolute discretion to "distribute in whole or in part, the Trust Property to the Beneficiary at any time and in such manner or amount as he may deem the situation to warrant . . . [and] the Trustee shall nevertheless be free to distribute the Trust Property or any part thereof . . . should what the Trustee deems a special emergency arise." The trusts also provided that any accumulated income not distributed became a part of corpus and was subject to the same limitations and powers as the corpus originally placed in trust.. In an estate tax proceding, *Held*: "The decedent [father], by creating the trusts, transferred to himself as trustee the right to receive the income from the corpus without any financial benefit to himself individually, but reserved the right to determine when and how each beneficiary should enjoy the income and thereby reserved to himself a 'power to alter, amend, or revoke,' within the meaning of the provisions of Section 811(d)(2)."

Tax-Exempt Bonds Are Nevertheless Subject to Inclusion in Gross Estate

Greene and Wells Fargo Bank & Union Trust Co. v. The United States, United States Court of Claims, March 4, 1959

Executors sought a refund because of the inclusion in decedent's gross estate of United States 3% Panama Canal loan bonds. Both the statute authorizing the bond issue and the bonds themselves stated that the bonds were "exempt from all taxes or duties of the United States, as well as from taxation in any form by or under State, municipal or local authority." *Held*: "We hold that the words 'taxes' and 'duties' as used in the statute involved in the instant case and as used in the bonds issued thereunder were meant by the Congress to exempt the principal and interest of such bonds from taxes levied by the United States, as well as taxes levied by any State, municipality, or local authority, and were not intended and did not have the effect of exempting a decedent's gross estate from estate taxes, which are a tax not upon the property itself, but upon the transfer or shifting of ownership of such property."

Situation at Death Rather Than at Time of Gift Determines Taxability

The Bridgeport-City Trust Co. v. Sullivan, Connecticut Supreme Court of Errors, January Term, 1959

During his life decedent established two trusts for certain relatives, with income and specified portions of principal to the beneficiaries for their lives and remainder as the beneficiaries should appoint by will. In the absence of such appointment, the trust remainders were to go to the beneficiaries' heirs at law. Decedent paid gift taxes on the trusts, and thereafter assigned to a charity all the interest which he had or might have in the trust properties. The tax commissioner argued that because decedent was a relative of the beneficiaries it would have been possible for him to inherit trust property from some or all of the beneficiaries if he had survived them and, therefore, that the transfers are taxable as gifts intended to take effect in possession or enjoyment at or after decedent's death. *Held*: No succession tax is due on the value of the trusts. "In the case before us, any possibility that any part of the corpus of the trusts could revert to the settlor was dissipated by the assignments he executed in 1947 in favor of the hospital. Any doubt that the settlor intended, at the times he created the trusts, to divest himself completely of every possibility of reversion was removed by these assignments. It is the state of affairs at the time of the decedent's death, as distinguished from the situation at the time the transfers were made, which determines, at least in this case, the question of taxability. We view the sequence of events in the order of the actual rather than the possible."

Estate Tax Marital Deduction is Mandatory And May Not Be Waived

Revenue Ruling 59-123, I.R.B. 1959-15, p. 18

A husband died, and his wife died soon thereafter. The husband bequeathed all his estate to his wife, and, by reason of the estate tax marital deduction, his net taxable estate was zero and not subject to any estate tax. After the wife died the value of the interest passing to her from her husband's estate was included in her estate. Question arose whether the husband's estate could waive the marital deduction so that (1) the wife's gross estate would be reduced by the value of the marital deduction she in fact received and (2) the wife's estate would receive the benefit of the credit for the estate tax on the husband's entire estate. The above Ruling states that the marital deduction section of the Code is mandatory and "may not be waived by the estate of the first [of] two spouses to die . . . in order to obtain a Federal estate tax benefit otherwise authorized by the Code, or for any other purpose."

No Gift of Present Interest When Donor Specifies How Trust for Minor Can Be Distributed

Revenue Ruling 59-144, I.R.B. 1959-17, p. 14

A gift was made in trust for a minor. The trust instrument provided that income and corpus could be expended for the benefit of the minor until he reached 21, and at 21 the minor could either compel immediate distribution of corpus or elect to continue the trust and receive one-third of corpus at age 25, one-third at age 29 and the final one-third at age 33. Section 2503(c) of the 1954 Code provides that a gift to a minor is a gift of a present interest if the property will pass to the minor at age 21 or to his estate or his appointees if he dies before reaching 21. Section 25.2503-4 (b) (2) of the gift tax regulations provides that the gift is still one of a present interest even though the minor, on reaching 21, has the right to extend the term of the trust. Question arose whether the gift in trust was a gift of a present interest which qualifies for the federal gift tax annual exclusion. The above Ruling states that the gift in this case was not a gift of a present interest and does not qualify for the annual exclusion. "The [above gift tax] regulation was designed to permit the extension by the donee of the terms of the trust upon such condition as the donee may freely choose. It was not designed to permit extension of the trust upon conditions set forth by the donor in the trust instrument. The basic purpose of the statute is to allow the statutory exclusion if the property involved in the transfer to the minor-donee will pass to him as absolute owner upon his reaching age 21. To permit the donor to set forth conditions under which the property may be handled after the donee reaches age 21 would be inconsistent with absolute ownership by the donee and, hence, inconsistent with the purpose of the statute."

Substantial Present Economic Benefit is Test For Determining a Taxable "Enjoyment" of Property

Estate of McNichol v. Commissioner of Internal Revenue, United States Court of Appeals, Third Circuit, April 17, 1959

By written instrument a father transferred real property to his children. By subsequent oral agreement with the children he continued to receive the income from the property until his death and took all available income tax deductions applicable to the property. After the father died his executors advanced this argument: Since under applicable state law the oral agreement was unenforceable, and since the children owned the property absolutely by written deed, the father had no "right" to the income and, therefore, he had not in fact retained for his life the possession or enjoyment of the property transferred; accordingly, the value of the property transferred should not be included in his gross estate. *Held*: "The conclusion is irresistible that the . . . decedent 'enjoyed' the properties until he died . . . He who receives the rent in fact enjoys the property. Enjoyment as used in the death tax statute is not a term of art, but is synonymous with substantial present economic benefit. . . . Under this realistic point of view the enjoyment of the properties which the decedent conveyed to his children was continued in decedent by prearrangement and ended only when he died."

TRUST DECISIONS

Digest of current decisions pertaining to the law of trusts, wills, estates, descent, distribution and corporate fiduciaries

Failure to Object to Accounting Defeats Attempt to Surcharge

Estate of Hart, California District Court of Appeal, Third District, November 25, 1958

The estates of deceased spouses became involved in litigation over the ownership of certain property standing in the wife's name. In a separate proceeding the wife's administratrix inventoried the disputed property, included it as estate assets in her accounting and had the account, including payment of attorneys' fees and the administratrix' commissions, judicially approved. The husband's estate neither objected to nor appeared in the accounting proceeding. Thereafter it was determined in the original litigation that the disputed property belonged to the husband and that it should be paid over to the husband's representative. The amount available for payment, however, was insufficient to cover the value of the property because of depletion for payment of administration expenses. An action was brought to surcharge the wife's administratrix for the deficiency. *Held*: The wife's administratrix cannot be surcharged. The husband's representative should have objected to the final account of the wife's estate as an interested party entitled to certain estate assets. By failing to do so, he is now left without a remedy.

Mere Right to Withdraw From Another's Account Does Not Create Joint Ownership

Jones v. Neu, Ohio Court of Appeals, May 29, 1958

A mother opened two savings accounts on the same day, one in her name, the other in her son's. She also executed a document authorizing the son to withdraw from the account in her name "such sums as he may call for." Subsequently the son withdrew the balance in the mother's account and transferred it to the account in his own name. After the mother died, her administrator sought to recover such balance as constituting an estate assets. *Held*: The son's authority with respect to his mother's account was limited to the right to withdraw. This authority made him only an agent for his mother and did not create a joint ownership of the account. The balance in the mother's account at the time it was withdrawn is an asset belonging to her estate.

Second of Two Irreconcilable Will Provisions Controls

Estate of Mayer, New York County Surrogate's Court, 141 New York Law Journal 13, February 19, 1959

Paragraph 13 of a will provided that the executors were authorized to invest estate funds in legals. Paragraph 14 authorized the executors to "sell, mortgage, lease or convey any or all of my property at public or private sale, at any time or any place and for any price and upon any terms as to cash or credit, as they in their discretion shall deem proper. I hereby vest in [them] all powers in respect to the sale, disposal, investment or re-investment of my estate, which I may have personally exercised, if living." In a construction proceeding, *Held*: When absolutely necessary there can be invoked a rule of judicial construction whereby the second of two irreconcilable provisions in a will be given total effect to the exclusion of the first. "This appears to be a situation of that kind, for in conferring upon his executors unlimited investment authority in paragraph fourteenth the testator clearly extended their authority beyond the limits he had fixed in paragraph thirteenth. Under the circumstances the court is constrained to hold that paragraph fourteenth controls."

Substituted Securities Need Not be Legals if Original Corpus Consisted of Non-Legals

In re Bankers Trust Company, New York County Supreme Court, 141 New York Law Journal 12, March 5, 1959

Corpus of a trust, of which the settlor was trustee, consisted of stock in a real estate investment company. In the event the real estate company was dissolved or reorganized so that either money or "some other security" was substituted as corpus, the trustee and his successors were authorized to invest in "such form of securities as in my or their discretion will yield the largest income consistent with the safety of the principal or to continue to hold said substituted securities." In a construction proceeding, *Held*: "The authorization to reinvest in securities warrants the inference of authority to invest in securities of a type similar to those contributed to the trust corpus which was composed of non-legals. Furthermore, such a directive is consistent with an intent not to restrict the trustee to legals only, on which as attractive a return was not possible at the time of the creation of the trust. The use of the words 'yield the largest income consistent with the safety of the principal' indicate a grant of discretion to the trustee as to investments and takes it out of the zone of strictly legal investments."

General Legatee Neither Loses Original Bequest of Stock Nor Gains Additional Shares Resulting From Stock Split

Cuppett v. Neilly, West Virginia Supreme Court of Appeals, November 11, 1958

Testatrix's will bequeathed a legatee 100 shares of stock and a bond. Due to a subsequent stock split testatrix actually owned 250 shares of the stock when she died. The legatee claimed that he was entitled to all 250 shares, as well as to the interest accruing on the stock and the bond since testatrix's death. *Held*: In the absence of a contrary intention expressed in the will, the bequest of the stock and bond were general legacies rather than specific legacies. Since the bequest of stock was a general legacy it is not revoked by the change in the number of shares testatrix owned at her death, but by the same token, neither can the bequest be more than the original 100 shares. The stock and the bond being general legacies, and thus general assets of the estate, the legatee is not entitled to interest on the securities until they are transferred to him in distribution of the estate.

Executor Who Doesn't Qualify Entitled to Reimbursement for Probate Expenses

Estate of Lewis, Tennessee Court of Appeals, December 31, 1958

A named executor was successful in having the will admitted to probate in a contested proceeding. After the will was probated the executor refused to qualify because of ill health, but he did seek reimbursement from the estate for attorneys fees incurred by him in the probate litigation. *Held*: It was the named executor's statutory duty to defend and establish the will, and he is entitled to reimbursement for legal fees incurred in the performance of such duty. His subsequent renunciation of his appointment in no way defeats his right to reimbursement.

INVESTMENT AND FINANCE

Edited by OSCAR LASDON

The Tax Structure and Stock Prices

"THE corporate tax structure, together with personal income taxes and capital gains taxes, has the simultaneous effect of limiting the supply of stocks while increasing the demand for them." This observation was made at the recent ABA Southern Trust Conference by Charles W. Buek, executive vice president of the United States Trust Company of New York.

From the corporate management point of view, Mr. Buek explains, there are two good reasons for preferring to attract capital funds through borrowing rather than through sale of new stock. Interest on short or long term debt is deductible in the corporate income tax return; furthermore, the widening practice of offering stock options and various types of stock purchase plans appears to prejudice some managements against the sale of additional shares. This situation prevails even though corporate shares are quoted at extraordinarily high multiples of earnings. For a while, there was some belief that the relationship of interest rates to dividend rates would bring the situation back to normal, but the disparity persists.

Tax considerations also guide the individual investor in his choice of common stocks for investment. Capital gains taxes often affect his decision in not one, but two ways. A wealthy investor prefers appreciation at the tax rate applicable to capital gains rather than dividends which are subject to a higher rate of tax. In extreme cases, observes Mr. Buek, this policy is carried so far that individuals actually avoid dividend income and have a preference for companies paying a poor dividend. This preference tends to prolong the period of low common stock dividend yields.

Large holdings of low-cost stocks in individual hands have been effectively removed from the market by capital gains taxes. "Although we investment managers tell our customers that the avoidance of capital gains taxes is never a sufficient reason to retain a stock," says the U. S. Trust Company officer, "the fact remains that many holdings are becoming more firmly glued to the bottom of the box with every point of increase in the Dow Jones averages. A long list of fine stocks such as General Electric and DuPont were undoubtedly available for sale in 1939 when the taxable profit was small, and might even have been pried loose from their owners at the level of the stock market in 1949. Paradoxically, they are less likely to be sold in 1959 than ever before, and every added point in the averages merely deepens the freeze. This may not represent good investment judgment, but it is nevertheless a fact.

"All this leads us to believe that we may be faced with a chronically high stock market for so long a period ahead that we shall have to learn to live with it. I do not mean that it will not fluctuate downward," continues Mr. Buek, "for a thorough-going correction is long overdue, but it seems more than likely that good stocks will sell at higher multiples of earnings in the future than they did when we were first learning the investment game. This means that we must face the prospect of more limited dividend returns than we were once able to acquire."

How Not to Invest Trust Funds

Factors which should *not* be permitted to control trustees' investment decisions were outlined by Guerry Snowden, vice president of the South Carolina National Bank of Greenville, S. C.

1–The whim, desire, or opinion of a trust beneficiary or member of his family. Information with respect to an investment is frequently picked up from non-qualified sources and may be just as frequently accompanied by assurances from the grantor, that he, the beneficiary and all others having interests in the trust will agree to the purchase; that they would never criticize the trustee for having purchased the particular issue, and therefore, there should be no reason for the trustee to hesitate on the purchase.

There are two flaws in this reasoning. In many trusts, it is not always possible to identify all who have an interest; an untimely or unexpected death of a remainderman may bring others into the picture who can later criticize the trustee or who may suffer from such investment decisions. Furthermore, where investment authority is solely vested in the trustee, it is logical that the investment decisions should be exclusively his own.

2–Tax factors should not be permitted to completely control the investment program. On many occasions, there is a reluctance to make sound investment changes because of the resulting income tax liability. On other occasions, there is an eagerness to take losses for tax purposes even though investment considerations do not warrant disturbance of the investment.

3–"Fashion" should not be permitted to determine investment policies or decisions. One pertinent illustration of such a fashion was the rush to buy turnpike bonds several years ago.

4–Every effort should be made to avoid an arrangement in which the trustee appears to have full investment authority but, nevertheless, has to clear with some one else. This sometimes happens in pension and profit-sharing trusts, where investment recommendations of the trustee must be cleared through an advisory or administrative committee before orders can be executed. It also occasionally happens in other trusts where the trustee recommends but, before acting, is required to clear with the grantor, his lawyer, his wife or some other person.

This is an unwholesome state of affairs at any time. The trouble with this type of investment provision is that, for all practical purposes, the trustee has full responsibility but incomplete authority.

5–No investment decision, whether important or trivial, should be based on the convenience of the bank or the accommodation of a commercial bank customer.

6–Following the line of least resistance should be avoided. All rights to subscribe to new shares of stock, for example, should not be treated alike.

7–Impressive but incomplete information should not be accorded undue weight.

Mr. Snowden proffered this valu able prophylactic advice at the recent Southern Trust Conference of the American Bankers Association

Life Tenant v. Remainderman

Back in 1831, in the well-known case of *Harvard College v. Amory,* a rule of law and standard of conduct were enunciated by Judge Putnam of the Supreme Judicial Court of Massachusetts. As all attorneys are aware, this decision concerned itself with how a trustee was to invest. On the other hand, the law has given little assistance in the face of a conflict of interests –such as that which exists between life tenants and remaindermen.

There are some areas, it is true, where this type of conflict can be disposed of by a decision, one way or the other. In this category fall those cases where the conflict turns on an issue of law which, if serious enough, the trustee takes to court. Certainly, with respect to the extent of the trustee's powers, this is a matter for court decision, just as one court would ask a higher court to determine a question of its own jurisdiction.

But what really bothers a trustee "are the conflicts which cannot be decided but must be resolved or reconciled, or if neither is possible, compromised." This is pointed out by Charles P. Curtis of the Massachusetts Bar in his illuminating monograph, "The Modern Prudent Investor–How to Invest Trust Funds." Mr. Curtis airs the distinction between contraries and subcontraries, adding that logicians know the difference.

"Contraries are one thing," he notes. "You have to choose one or the other. Subcontraries are another thing. The more there is of one, the less there is of the other. You don't choose, you mediate. You reconcile them if you can. You compromise them if you can't."

Majority of the conflicts between life tenants and remaindermen are in the subcontrary category. In almost every investment the trustee makes, and in almost every investment policy he pursues, the issue of favoring arises. Is the life estate or the remainder favored, in which way, and how much?

"It is only when you extrapolate subcontraries," remarks Mr. Curtis, "that the choice of an answer between subcontraries is like a choice between contraries." In this connection, the specific word of his selection is "*accommodate*, because the conflict is seldom one that can be decided and disposed of, as a judicial decision disposes of a case."

Worth remembering is the author's thought that "No trustee, whatever his efforts, can eliminate the conflict, and he would do well not to try. He had better try to illuminate. . . ."

The "Modern Prudent Investor" is one of three noteworthy monographs recently published by the Committee on Continuing Legal Education of the American Law Institute and the American Bar Association. Companion volumes of great practical value are the "Federal Securities Act Handbook," by Eliot B. Thomas and "Buying, Selling and Merging Businesses," by Allen D. Choka. Individual copies may be obtained at a cost of $3.00 from the Director of the Committee, 133 South 36 Street, Philadelphia 4, Pa.

Treasury Debt Limitations

Facts relating to the interest rate ceiling on the Federal debt, as well as the dollar amount ceiling, are set forth in an interim bulletin released by the Economics Department of the Bankers Trust Company of New York City.

Operation of a legal provision, dating back to World War I, appears to bar the Treasury from issuing bonds bearing more than 4¼ per cent interest. Under the Third and Fourth Liberty Bond Acts, enacted in 1918, this was the maximum authorized rate on the statute books. However, it should be noted that this rate ceiling applies exclusively to bonds; it does not apply to Treasury bills and certificates, which mature in one year or less, nor to notes, which are issued for periods of one to five years.

The Bankers Trust bulletin also points out that, in World War II, the Public Debt Act of 1942 authorized the Secretary of the Treasury to issue any obligations as he might prescribe. Nevertheless, despite this apparently broad authority, the weight of opinion seems to be that it was not the intent of Congress to abrogate the 4¼ per cent interest rate ceiling.

With respect to the debt ceiling figure, this now stands at a temporary $288 billion, but is scheduled to revert to the permanent level of $283 billion by July 1,—a level which will undoubtedly have to be raised by the time this department is in print. Last January, the Budget Message estimated that debt subject to the ceiling would be almost $285 billion on June 30, or nearly $2 billion above the permanent limit. And since the major portion of tax receipts accumulates in the first half of each calendar year, sizable borrowings will be necessary to cover the operating deficit in the July-December, 1959 period.

During the past several years the Treasury, in operating near the debt ceiling, has been compelled to resort to makeshift devices to hold the debt below the limit. As the Bankers Trust Company observes, this has forced the Treasury to raise funds indirectly through security issues of the Federal National Mortgage Association or certificates of indebtedness of the Commodity Credit Corporation. On two occasions, the Treasury had to draw on its "free" gold in order to remain within the statutory debt ceiling.

Odds and Ends

"Concentration and Competition in New England Banking" by Paul M. Horvitz, is the title of a special research report being made available by the Federal Reserve Bank of Boston.

The New York Stock Exchange "Fact Book" for 1959 can be obtained by directing a request to 11 Wall Street, New York City.

"The Story of Modern Home Financing," a layman's guide to "Why, what and how of home financing," may be obtained from the United States Savings & Loan League, 221 N. LaSalle St., Chicago 1, Ill. Also available is a report on the characteristics of single family house buyers, "Who Buys the Houses."

The Amos Tuck School of Business Administration, Dartmouth College, Hanover, N. H., has announced the availability of its most recent booklet in its business and economic series, "Economic Indicators."

"Timely Notes on Instalment Credit", published by the Instalment Credit Commission of the American Bankers Association, reviews current trends and developments and also discusses revolving check credit. The New York City office of the ABA is located at 12 E. 36 Street.

BOOKS FOR BANKERS

LECTURES IN FINANCIAL MANAGEMENT. By R. M. Soldovsky. Iowa Book and Supply Co., Iowa City, Ia. 1958. $2.50. Pp. 118. Professor Soldovsky's collection of lectures provide practical and pointed assistance in the area of financial management. The discussion material is very meaty and accomplishes a maximum of education through the use of specific case illustrations. Fifteen lectures are reproduced, each of which leaves the reader with a high degree of orientation.

CORPORATIONS, CASES AND MATERIALS. Third Edition, with supplement. By Ralph J. Baker and William L. Cary. Foundation Press. Brooklyn, N. Y. 1958-59. $13.50. Pp. 1536. This casebook needs no introduction to members of the legal fraternity. It spreads wide, covers much, and does it exceedingly well. The chapter on "Control and Management of the Corporation" includes extensive new material pertaining to special problems of the close corporation, the contrasting problems of the publicly held company under the proxy system, and policy and practitioners' views toward cumulative voting and drafting voting trusts. "Financing the Corporation" also is almost entirely new material and is aimed at developing some instinct for planning. Corporate distributions, mergers, shareholders' derivative suits are among the other areas receiving unusual treatment. The excellence of this work is evident.

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Photograph by Harold Halma

A boy keeps days like these all his life. Some day he'll trundle his own sons in a barrow too—remembering the jolly, peaceful man-to-man times spent with his father.

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